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No. 86-422

In the Supreme Court of the United States

OCTOBER TERM, 1986

DAVID CARPENTER, KENNETH P. FELIS, AND R. FOSTER WINANS, PETITIONERS

v.

UNITED STATES OF AMERICA

ON WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SECOND CIRCUIT

BRIEF FOR THE UNITED STATES

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QUESTIONS PRESENTED

1. Whether petitioners' trading in securities on confidential, market-affecting information that had been misappropriated in breach of a duty of trust and confidence violated the mail and wire fraud statutes, 18 U.S.C. 1341 and 1343.

2. Whether petitioners' trading in securities on this misappropriated information violated Section 10(b) of the Securities Exchange Act of 1934, 15 U.S.C. 78j(b), and Rule 10b-5, 17 C.F.R. 240.10b-5.

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BRIEF FOR THE UNITED STATES

OPINIONS BELOW

The opinion of the court of appeals (Pet. App. 1a-29a) is reported at 701 F.2d 1024. The opinion of the district court (Pet. App. 33a-73a) is reported at 612 F. Supp. 827.

JURISDICTION

The judgment of the court of appeals was entered on May 27, 1986. Petitions for rehearing were denied on July 17, 1986. The petition for a writ of certiorari was filed on September 15, 1986, and was granted on December 15, 1986. The jurisdiction of this Court is invoked under 28 U.S.C. 1254(1).

STATUTES INVOLVED

The texts of 15 U.S.C. 78j(b), 18 U.S.C. 371, 1341 and 1343, and 17 C.F.R. 240.10b-5, are set out in an appendix to this brief.

STATEMENT

Petitioners engaged in a scheme to trade in securities on market-affecting information that was the property of The Wall Street Journal. Petitioner Winans, a writer for the Journal, misappropriated confidential

information about forthcoming Journal articles that were expected to—and did—affect the prices of securities discussed in the articles; Winans, petitioner Felis, a stockbroker, and petitioner Carpenter used that information to buy and sell securities before publication of the articles. After a bench trial in the United States District Court for the Southern District of New York, Felis and Winans were convicted of conspiracy to commit fraud and to obstruct justice, in violation of 18 U.S.C. 371; they were also convicted, together with Carpenter, of securities fraud, in violation of 15 U.S.C. 78j(b) and 78ff, 17 C.F.R. 240.10b-5, and 18 U.S.C. 2; mail fraud, in violation of 18 U.S.C. 1341; and wire fraud, in violation of 18 US.C. 1343.

1. a. Petitioner Winans was hired by the Dow Jones News Service in March 1981. In the summer of 1982, Winans became one of the two full-time writers responsible for The Wall Street Journal's "Heard on the Street" column (*Heard* column). Pet. App. 35a. This feature, which was regarded by Journal editors as "one of the most important" and "sensitive" of the newspaper's columns (C.A. App. A118), was characterized by the district court as "a daily market gossip feature, which highlights a stock or group of stocks and analyzes notable volumes of trading or price movements occurring in the

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[1] Carpenter was sentenced to concurrent terms of three years' probation and to concurrent $1,000 fines on six counts of securities fraud, three counts of mail fraud, and three counts of wire fraud. Winans was sentenced to concurrent terms of 18 months' imprisonment on one count of conspiracy, five counts of mail fraud, and five counts of wire fraud; he was also assessed concurrent $5,000 fines on the conspiracy count and on each of five counts of securities fraud, as well as concurrent $1,000 fines on five counts of mail fraud and five counts of wire fraud, and was placed on five years' probation. Felis was sentenced to concurrent six month sentences on one conspiracy count and on five counts each of securities, mail, and wire fraud; he was also fined a total of $25,000 (specifically, fines of $10,000 on the conspiracy count, $5,000 on one count of securities fraud, and $1,000 on each of five counts of mail and wire fraud), and was placed on five years' probation.

market" (Pet. App. 35a). The *Heard* column "also takes a point of view with respect to investment in the stocks that it reviews" (*ibid.*). Both courts below found that the column has a predictable—and at times dramatic—short-term effect on the prices of the securities it discusses (*id.* at 19a n.9, 35a-36a). Winans and the other petitioners understood the column to have such an impact on the market (*id.* at 36a).

b. When Winans was hired by the Journal he was informed of the conflict of interest policy maintained by Dow Jones & Co., the Journal's publisher. Compliance with that policy (see J.A. 39-43), which has been promulgated to forestall employee actions "detrimental to the best interests of Dow Jones" (*id.* at 39), was labelled "essential" to avoid "the tremendous embarrassment and damage to the Company's reputation that could come about through [an employee's] lapse in judgment" (*id.* at 41; see *id.* at 43). To this end, the policy flatly prohibited Journal employees from disclosing information about the subject or publication date of forthcoming articles, and from trading securities in anticipation of the appearance of those articles. The policy stated:

> First and foremost, all material gleaned by you in the course of your work for Dow Jones is deemed to be strictly the Company's property. This includes not only the fruits of your own and your colleagues' work, but also information on plans for running items and articles on particular companies and industries and advertising schedules in future issues. Such material must never be disclosed to anyone outside the Company, including friends and relatives.

J.A. 41-42; see *id.* at 40. The policy went on to provide that "[n]o employee with knowledge of a forthcoming article, item or advertisement concerning a company or industry should, prior to the publication of such article, item or advertisement, invest in that company or companies in that industry;" employees were instead directed to avoid dealing in the securities of the company involved for two full trading days, "until the general public has

an opportunity to read and digest the information" (*id.* at 42).[2] Because compliance with these rules was understood to be critical to the preservation of Dow Jones' reputation, the statement indicated that "any slip in judgment in * * * [areas] covered in this policy statement [is] serious enough to warrant dismissal" (*id.* at 41).

During Winans' tenure at the Journal, the newspaper took other steps as well to emphasize the importance of, and to insure compliance with, the Dow Jones policy. At least two Journal editors personally reminded Winans early in his employment "of the confidential and sensitive nature of the *Heard* column" and emphasized "the importance of not investing in stocks the writer is covering." These editors subsequently gave Winans "follow-up reminders about the confidentiality of the column." Pet. App. 36a. In February 1984, the Journal's managing editor and New York bureau manager issued a directive to all employees reiterating that "[w]e don't ever tell anyone outside the paper when or if a story is going to run or what it is going to say. Ever" (C.A. App. A108). The district court found that "Winans had actual knowledge of the policy with respect to maintaining confidentiality of the column," "knew that part of his job responsibilities were to keep the subject matter and publication date of the column secret," and "knew that he was supposed to tell his editors if he heard that word was out about a column's topic" (Pet. App. 37a). Winans also knew that he would be fired if he was caught trading in the stock of companies mentioned in

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[2] The policy also indicated that employees were "expected" to "avoid any action, no matter how well-intentioned, that could provide grounds even for suspicion" that they "made financial gains by acting on the basis of 'inside' information obtained through a position on our staff, before it was available to the general public. Such information includes * * * our plans for running stories [and] items that may affect price movements * * *." Employees were also directed to avoid actions that might give rise to a suspicion "that the writing of a news story or item * * * was influenced by a desire to affect the stock's prices." J.A. 40-41.

the *Heard* column or disclosing information about forthcoming columns (*ibid.*).[3]

2. a. In October 1983 Winans entered into a scheme with two stockbrokers at Kidder, Peabody & Co. (Kidder), petitioner Felis and Peter Brant, to trade on his knowledge of forthcoming *Heard* columns. The three agreed that Winans would leak information to the brokers about "the timing, subject and tenor" of soon-to-be-published columns. Armed with this knowledge—and their awareness of the *Heard* column's market impact—the brokers would then buy or sell the securities of the companies to be discussed in the column. The profits would be split among the conspirators. Pet. App. 40a.

Over the next five months, Winans leaked information about approximately 27 *Heard* columns, including columns that he had written and columns written by other Journal reporters.[4] When the topic was set for the fol-

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[3] At trial, Winans denied knowledge of the Journal's policy and testified that he was not informed of the confidentiality of the *Heard* column by his editors (see Pet. App. 36a). The district court, however, specifically "accept[ed] the testimony" of Winans' editors to the contrary, and found "incredible Winans[']' denial that he ever received the conflicts of interest policy statements" (*id.* at 37a).

[4] Both Brant and Winans testified that it was part of their original scheme "that the arrangement would not affect the journalistic purity" of Winans' writing (Pet. App. 40a). The district court, however, noted Winans' testimony before the Securities and Exchange Commission that the "promise of a big distribution of profits" from Brant "was 'an inducement' and a factor in his choosing" to write about a certain stock. While Winans later testified that he in fact exercised independent journalistic judgment in deciding to write the column in question, the district judge did "not accept [Winans'] rejection of his SEC testimony; rather, [the judge] accept[ed] it as evidence of Winans' criminal intent." *Id.* at 45a. While the court found that several others of Winans' columns appeared to be unaffected by the conspiracy, it noted "the difficulty of maintaining a stance of journalistic purity when the reporter is engaged in a decidedly unpure venture" (*id.* at 44a (footnote omitted)). In any event, the court concluded that "[m]aintaining the journalistic purity of the column was actually consistent with the goals of the conspirators" because "a particu-

lowing day's column, Winans would call Brant or Felis with that information. As the district court explained, "[d]epending on the positive or negative tone of the article, stock was either bought or sold short, and call or put options were either bought or sold. Most often, the transactions were closed on the same day as an article's publication, thereby maximizing its impact." Pet. App. 42a. Winans also used his knowledge of forthcoming *Heard* columns to complete six trades for the account of his friend, petitioner Carpenter, who "was aware that these purchases and sales were connected with the appearance of articles in the Journal" (*id.* at 45a).[5] In all, the scheme netted its participants profits of approximately $690,000 (*id.* at 42a).

b. During the course of the scheme, petitioners adopted elaborate strategems to avoid detection by the Journal or public authorities. Winans objected to meeting with Felis or Brant in places where he might be seen by Journal employees or Wall Street acquaintances; he telephoned the two brokers from empty Journal offices or outside pay phones and frequently used a false name when identifying himself to Brant's secretary (Pet. App. 7a, 42a, 44a). Felis and Brant in turn paid Winans his share of the trading profits by checks made payable to Carpenter. To support a cover story that those checks represented payments for decorating services, Felis wrote the word "drapes" on a $10,000 check, and Carpenter subsequently provided Brant and Felis with false invoices for decorating services. *Id.* at 7a, 40a, 43a, 47a-49a.

Petitioners and Brant continued trading in securities even after their activities had aroused suspicion. When questioned by Kidder's Regional Manager in November

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larly compelling column or a fresh investment thesis would have a significant impact on the price of the featured stock" (*id.* at 44a n.4).

[5] Carpenter, a former Journal news clerk, was generally aware of the Dow Jones policy (Pet. App. 37a-38a). In addition to the profits he obtained from the trading in his account, Carpenter acted as a messenger between the conspirators (*id.* at 5a-6a).

1983 about a correlation between their trading and the *Heard* columns, Felis and Brant lied about the source of their information. After being told to stop their trading, they liquidated Felis's existing account but opened a Swiss bank account in the name of a Costa Rican shell corporation through which they continued to trade on Winans' information. Pet. App. 7a, 46a. As investigations into their activities continued, Winans, Felis and Brant repeatedly lied to the Securities and Exchange Commission (SEC), the Journal, and Kidder about the nature both of their trading and of their relationships with one another (*id.* at 7a, 47a-48a). Petitioners and Brant also made efforts—ultimately unsuccessful—to coordinate their deceptive stories (*id.* at 48a-49a).

3. Petitioners were convicted following a 20-day bench trial. In finding petitioners guilty of securities fraud, the district court explained that " 'one who misappropriates nonpublic information in breach of a fiduciary duty and trades on that information to his own advantage violates Section 10(b) [of the Securities Exchange Act of 1934, 15 U.S.C. 78j(b)] and Rule 10b-5 [17 C.F.R. 240-.10b-5]' " (Pet. App. 53a (citation omitted)). The court noted that this "misappropriation theory" of securities fraud finds support in the concurring and dissenting opinions in *Chiarella* v. *United States*, 445 U.S. 222 (1980), and is firmly rooted in Second Circuit precedent (Pet. App. 52a-55a). In this case, the court added, "Winans knew he was not supposed to leak the timing or contents of his articles or trade on that knowledge. * * * Winans breached the [Dow Jones] policy and he knew he was breaching it" (*id.* at 58a-59a).

The district court also held that petitioners had committed mail and wire fraud, explaining that Winans' breach of duty and failure to notify the Journal about leaks of the *Heard* column defrauded his employer. The court noted that "Winans' disclosures can only be seen as an abuse of his employers' confidences since he owed a fiduciary duty to the Wall Street Journal not to disclose the contents of the [*Heard*] column in advance"

(Pet. App. 61a); Winans was "aware[] that he had a duty not to disclose the content and timing of publication of the column as well as a duty to disclose, at the very least, any leaks of the column" (*id.* at 62a). The court also found that the scheme contemplated actual harm to the Journal: petitioners' activities "placed immediately in jeopardy probably [the Journal's] most important asset—its reputation for fairness and integrity" (*id.* at 64a). The court thus found that "[t]he scheme's injurious consequences to the Journal must have been known to Winans" (*ibid.*) and to the other participants (*id.* at 64a-65a). Similarly, the court held that the telexing of articles for printing and the mailing of the Journal to subscribers were "integral part[s] of the scheme to defraud" (*id.* at 66a). And the court found that Winans and Felis acted with specific intent to deceive and defraud the Journal (see *id.* at 68a-69a, 71a-72a).[6]

4. In relevant part, the court of appeals affirmed petitioners' convictions.[7] Addressing the securities law counts, the court found that Winans "breached a duty of confidentiality to his employer by misappropriating from the *Journal* confidential prepublication information" (Pet. App. 10a), an action that "sull[ied] [the Journal's] reputation and thereby defraud[ed] it 'as surely as if [petitioners] took [its] money'" (*id.* at 18a (citation omitted)). This misappropriation, the court continued,

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[6] Petitioners assert that "neither Winans, Brant, nor Felis believed that they were acting illegally" (Pet. Br. 4). The district court, however, expressly found otherwise. It determined that "Felis' conduct throughout demonstrates that he was a willful and knowing participant in what he understood was an unlawful venture" (Pet. App. 71a). The court also found that "Winans and Felis, together with Brant, each had the requisite specific intent to defraud" (*id.* at 72a). The court found that Carpenter aided and abetted the scheme with the awareness "that what Winans was doing was a fraud on the [Journal]" (*ibid.*; see *id.* at 73a).

[7] The court of appeals reversed Winans' conviction on several counts involving trading by Felis that was outside the scope of the conspiracy (Pet. App. 26a-27a).

ran afoul of Section 10(b) and Rule 10b-5, which "broadly proscribe[ ] the conversion by 'insiders' *or others* of material nonpublic information in connection with the purchase or sale of securities" (Pet. App. 11a (emphasis in original)); the court added that application of the misappropriation theory in this context serves generally to forestall fraudulent practices (*id.* at 13a) and furthers "Congress' stated concern for the perception of fairness and integrity in the securities markets" (*id.* at 13a-14a). And "the use of the misappropriated information for the financial benefit of [petitioners] and to the financial detriment of those investors with whom [petitioners] traded," the court held, "supports the conclusion that [petitioners'] fraud was 'in connection with' the purchase or sale of securities under section 10(b) and Rule 10b-5" (*id.* at 18a).

The court of appeals found it unnecessary to "dwell at length on [petitioners'] convictions for violating federal mail and wire fraud statutes" (Pet. App. 23a). The court explained that confidential commercial information "may constitute fraudulently misappropriated 'property' under the mail fraud statute" (*ibid.*), and that petitioners' scheme to misappropriate nonpublic information from the Journal accordingly fell within the scope of 18 U.S.C. 1341 and 1343 (Pet. App. 24a). The court also concluded that the "foreseeability and centrality to the scheme" of the mailings and wirings associated with the publication and distribution of the Journal "were sufficient predicates to allow a conclusion that [petitioners] violated the mail and wire fraud statutes" (*id.* at 25a).[8]

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[8] Judge Miner joined the court's opinion insofar as it upheld petitioners' convictions on the mail and wire fraud counts, but he dissented from the court's holding on securities fraud (Pet. App. 27a-29a). He reasoned that "[n]o confidential securities information imparted by reason of any special relationship was purloined by [petitioners]," concluding that petitioners' "conduct is addressed adequately by statutes establishing the mail and wire fraud offenses of which [petitioners] stand convicted" (*id.* at 28a, 29a).

SUMMARY OF ARGUMENT

A. Petitioner Winans *posed* as a loyal employee of The Wall Street Journal. That deception afforded him continuing access to the Journal's confidential information, which he and the other petitioners used to trade securities. His trading violated his duties to the Journal and knowingly endangered the very asset of the newspaper that made the scheme work—the Journal's reputation for reliability and integrity. Winans' present pose as a newspaperman who happened to traverse the idiosyncratic workrules of a fussy employer is sheer nonsense.

Petitioners' conduct was more than the dishonest and ethically reprehensible action that they concede it to have been: it was a criminal fraud. It was well settled at the time of the enactment of the mail fraud statute in 1872, and it is equally clear today, that deceptive use of a relationship of trust and confidence with the victim, to gain advantage while knowingly harming or risking harm to the victim, is a fraud. Winans plainly had such a relationship with his employer. He fostered and carefully maintained a misimpression, on the part of the Journal, that he was a trustworthy employee and that the *Heard* column was not, to his knowledge, being leaked or misused. Petitioners used this misimpression and Winans' position of trust to gain access to a continuing flow of confidential information; that flow started because Winans made at least implicit representations of loyalty at the outset of his employment, and continued because Winans failed both to disabuse the Journal of its mistaken belief in the continuing validity of those representations and to comply with his specific duty to disclose leaks of the *Heard* column. And as petitioners well knew, their scheme to make money both relied on, and posed a substantial risk of harm to, an extremely valuable (albeit intangible) asset of the Journal, its reputation for reliability and integrity.

This scheme depended for its success on the publication of the *Heard* column, which required use of the mails

and interstate wires. Winans concededly caused use of the mails and wires when he delivered *Heard* columns to his editors with the expectation and intention that they be wired to the Journal's printing plant and mailed to the Journal's subscribers. Petitioners' contention that these transmissions would have occurred in the same form in the absence of the scheme is both unwarranted by the record and irrelevant: Winans caused the mailing and wiring of his columns with the pre-existing intention of using these particular columns (once transported) to commit a fraud. The scheme therefore violated 18 U.S.C. 1341 and 1343.

B. 1. Petitioners used their fraudulently misappropriated information to "'reap instant no-risk profits in the stock market'" (Pet. App. 19a-20a (citation omitted)). As four Justices of this Court (in *Chiarella* v. *United States*, 445 U.S. 222 (1980)), lower courts, and committees of Congress had concluded even prior to the events of this case, trading on misappropriated information violates Section 10(b) of the Securities Exchange Act of 1934 and Rule 10b-5 thereunder.

Petitioners' trading on fraudulently misappropriated information clearly falls within the broad language of the statute and rule: Section 10(b) makes it unlawful for "any" person, "directly or indirectly," to use "any" deceptive device in connection with the purchase or sale of "any" security, in violation of SEC rules; Rule 10b-5 proscribes "any" fraud upon "any" person in connection with the purchase or sale of "any" security. Here, petitioners committed a deliberate fraud upon the Journal, and the sole purpose of the fraud was to profit in securities trading. Beyond fidelity to the language, the prohibition of petitioners' trading on misappropriated information also serves both the Exchange Act's central purpose of "insur[ing] the maintenance of fair and honest markets" (15 U.S.C. 78b), and Section 10(b)'s particular aim of eliminating from securities trading all "manipulative and deceptive practices which have been demonstrated to

fulfill no useful function" (S. Rep. 792, 73d Cong., 2d Sess. 6 (1934)).

2. At certain points in their argument, petitioners seem to attack the misappropriation theory, suggesting that Section 10(b) proscribes only trading by "insiders" of the corporation whose stock is traded (who owe fiduciary duties to the persons on the other side of the transactions). But no decision of this or any other court has ever endorsed such a limitation on the scope of Section 10(b) or Rule 10b-5, which would be contrary to the language of the statute and rule. Such a limitation also would leave a large and illogical gap in the enforcement of the securities laws: it would permit persons who trade on information that is misappropriated from a tender offer bidder, from an investment banker advising a client about a possible investment in the subject company, or indeed from any party other than the company whose shares are traded, to go largely unpunished. Petitioners' related suggestion that in a public enforcement action the government must allege and prove injury to specified persons on the other side of the transactions has no basis in language, precedent, or logic.

At other points in their argument, petitioners appear to acknowledge that trading in the stock of one company on information fraudulently misappropriated from another is unlawful, but only (they say) if the third-party owner of the information is itself a "market participant," such as a takeover bidder. This limitation also finds no basis in language, precedent, or logic. While the misappropriation of information from a potential buyer or seller of securities may cause that person particular injury in connection with *its* purchases or sales of securities, the fundamental evil of trading on misappropriated information is that it "is unfair and inconsistent with the investing public's legitimate expectation of honest and fair securities markets where all participants play by the same rules." H.R. 98-355, 98th Cong., 1st Sess. 5 (1983). The use of such devices will drive investors out of the market, threatening both "[c]apital formation and our nation's economic growth and stabil-

ity" (*id.* at 2). Trading on misappropriated information inflicts a wound on the market and all who participate in it.

Petitioners' suggestion that they should not be convicted for trading that would have been lawful for Dow Jones is an attempt to throw sand in the Court's eyes. First, it is by no means clear, as the court of appeals noted, that a financial newspaper could make prepublication trades without violating Section 10(b) (albeit under a different theory than the one involved in this case). Second, there plainly are situations (such as pre-announcement purchases by a takeover bidder) where an owner of information is permitted, consistently with the language and philosophy of the securities laws, to trade on information that may not be misappropriated and used by an employee. Third, conversely, there is nothing anomalous about relying on the integrity and self-interest of the owner of the information (reflected in this instance by the very rules petitioners broke) to deter trading that is barred to a thief by a criminal statute such as Section 10(b).

ARGUMENT

PETITIONERS' MISAPPROPRIATION AND USE OF CONFIDENTIAL INFORMATION VIOLATED FEDERAL LAW

Petitioners' scheme was a classic fraud. Winans posed as a loyal employee of The Wall Street Journal, a deception that afforded him continuing access to confidential information; petitioners used that information to buy and sell securities in a manner that they knew endangered interests of the Journal. This sort of deceptive use of a position of trust is "as old as falsehood" (*Weiss* v. *United States*, 122 F.2d 675, 681 (5th Cir. 1941)), and as fraudulent. Because petitioners' scheme depended for its success on the use of the mails and interstate wires, it violated 18 U.S.C. 1341 and 1343. And because the purpose of the scheme was to " 'reap instant no-risk profits in the stock market' " (Pet. App. 19a-20a (citation omitted)) by trading with investors who "would

not have purchased or sold, at least at the transaction prices, had they had the benefit of that [improperly acquired] information" (*id.* at 18a), it violated the anti-fraud provisions of the federal securities laws as well.

A. An Employee Violates The Federal Mail And Wire Fraud Statutes When, In A Scheme That Requires Use Of The Mails And Interstate Wires, He Fosters And Maintains A Misimpression That Affords Him Access To His Employer's Confidential Information, Which He Uses To His Benefit And To The Employer's Detriment

The federal mail and wire fraud statutes, which in relevant part are identical, make it illegal to use the mails or interstate wires "for the purpose" of furthering "any scheme or artifice to defraud." 18 U.S.C. 1341, 1343.[9] It is common ground that the crimes defined by these statutes have two elements: a scheme to defraud (which contemplates some sort of harm to the victim), and a mailing or wiring. Both of those elements are abundantly present here. Petitioners' case is unusual, if at all, only in "the subtlety of the[ir] scheme" (*United States* v. *Bush*, 522 F.2d 641, 646 (7th Cir. 1975), cert. denied, 424 U.S. 977 (1976)).

1. *Scheme or artifice to defraud.* a. Sections 1341 and 1343 are written in broad terms. They apply to "*any* scheme or artifice to defraud," language that contains no explicit limits and that was drafted in a "sufficiently general" fashion to be applicable against novel or unanticipated forms of fraudulent conduct. *United States* v. *Maze*, 414 U.S. 395, 399 n.4 (1974). Indeed, Congress chose not to write an express definition of the term "fraud," and the term has resisted judicial definition; the courts have recognized, in Judge Holmes' famous phrase, that fraud is "as versable as human ingenuity" (*Weiss*, 122 F.2d at 681). But the concept of fraud nevertheless

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[9] As petitioners note (Pet. Br. 30 n.60), the mail and wire fraud statutes should be given a parallel interpretation. See, *e.g.*, *United States* v. *Lemire*, 720 F.2d 1327, 1335 (D.C. Cir. 1983) (citing cases), cert. denied, 467 U.S. 1226 (1984). References in this brief to either statute accordingly apply to both, unless differences are indicated.

has defined boundaries: it draws its content from the background of the mail and wire fraud statutes, and from a century of case law.

As the Court explained over 60 years ago, the hallmark of fraud is "trick, deceit, chicane or overreaching." *Fasulo* v. *United States*, 272 U.S. 620, 627 (1926). Certainly, as petitioners note (Pet. Br. 34), an explicit, affirmative misrepresentation about particular facts falls within this category of conduct. But so does a defendant's deliberately deceptive use of what the courts have called a relationship of "trust and confidence." When a defendant enters into such a relationship with the victim, feigns continuing loyalty, conceals his disloyal actions in violation of established disclosure obligations, and *uses* the resulting misimpression to his benefit and to the victim's detriment—for example, by obtaining continuing access to the victim's property or information, which he then misappropriates—the defendant has committed fraud. In such a case the defendant is able to benefit himself only because the victim trusted him, and because he allowed the victim to act under a misimpression about the nature of their relationship that he fostered and was under a duty to correct. These are the essential characteristics of a fraudulent breach of trust. See generally *Chiarella* v. *United States*, 445 U.S. 222, 227-228, 232 (1980); *id.* at 247 (Blackmun, J., dissenting); *SEC* v. *Capital Gains Research Bureau*, 375 U.S. 186, 193-194 (1963); Restatement (Second) of Torts § 551(2)(a) (1977); Keeton, *Fraud—Concealment and Non-Disclosure*, 15 Tex. L. Rev. 1, 11, 12-13 (1936); James & Gray, *Misrepresentation—Part II*, 37 Md. L. Rev. 488, 525 (1978) (cited in *Chiarella*, 445 U.S. at 228 n.9).[10] See also au-

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[10] While petitioners acknowledge that this sort of conduct may constitute a "constructive fraud" (Pet. Br. 33-34 & n.74), they argue that a breach of duty, when unaccompanied by an express misrepresentation, cannot give rise to criminal liability. But that proposition has been flatly rejected by this Court under the anti-fraud provisions of the securities laws. See *Chiarella*, 445 U.S. at 232. Indeed, under Sections 1341 and 1343, the courts of appeals have uniformly held that criminal liability may be imposed when

thorities cited at pages 20-21 note 16, 22, 24-25 note 23, *infra*.

The courts have long recognized that persons who assume positions of trust, undertaking to work loyally on another's behalf, commit "a major type of dishonesty" (*Post* v. *United States*, 407 F.2d 319, 329 (D.C. Cir. 1968), cert. denied, 393 U.S. 1092 (1969)) when they "obtain[] and then betray[] the confidence of another." *Shushan* v. *United States*, 117 F.2d 110, 115 (5th Cir.), cert. denied, 313 U.S. 574 (1941). *See United States* v. *Lemire*, 720 F.2d 1327, 1335 (D.C. Cir. 1983), cert. denied, 467 U.S. 1226 (1984).[11] The victim is, after all, as entitled to rely on the loyalty of those who hold themselves out as trustworthy as on arms' length representations made in the course of business. See 2 F. Harper, F. James & O. Gray, *The Law of Torts*, § 7.14, at 473-474 (2d ed. 1986). And one who enters a relationship of trust on the understanding that he will act in accord with certain rules, who continues in that position after delib-

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the defendant breaches a duty of trust with the intention of taking advantage of the principal, and when concealment and an intent to deceive are elements of the scheme. The crucial question is not whether the scheme involved an affirmative misstatement rather than a breach of duty, but whether the defendant intended to take advantage of—to defraud—the other party to the relationship. See *United States* v. *Ballard*, 663 F.2d 534, 541 n.17 (1981), modified on reh'g, 680 F.2d 352 (5th Cir. 1982); *United States* v. *Von Barta*, 635 F.2d 999, 1005 n.14 (2d Cir. 1980), *cert. denied*, 450 U.S. 998 (1981); *Epstein* v. *United States*, 174 F.2d 754, 766 (6th Cir. 1949). See generally Coffee, *From Tort to Crime: Some Reflections on the Criminalization of Fiduciary Breaches and the Problematic Line Between Law and Ethics*, 19 Am. Crim. L. Rev. 117, 122-123 n.30 (1981); Langevoort, *Fraud and Deception by Securities Professionals*, 61 Tex. L. Rev. 1247, 1252-1257 (1983). See also note 21, *infra*.

[11] As Professor Coffee notes in an article that is selectively quoted by petitioners (Pet. Br. 37), "a knowing fiduciary breach may be as egregious, injurious and deliberately fraudulent as the garden variety embezzlement." *From Tort to Crime: Some Reflections on the Criminalization of Fiduciary Breaches and the Problematic Line Between Law and Ethics*, 19 Am. Crim. L. Rev. 117, 149 (1981).

erately breaking those rules and failing to inform the other party of this change in the basis of their relationship, and who *uses* his position of trust to benefit himself at the other's expense, has indeed engaged in "trick, deceit, chicane, or overreaching." [12] What constitutes deception turns on context; if the victim allows the defendant to manage his business or obtain access to his property on a certain set of shared understandings, the defendant's failure to disclose his rejection of those understandings is recognized by the courts to be as fundamentally deceptive as an outright lie.

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[12] As one commentator has noted, "the fiduciary's failure to disclose material facts to a person who is entitled to rely on him is a tacit representation of the nonexistence of those facts." Similarly, one who misappropriates something with which he is entrusted violates his "implicit representation that he would not convert the thing to his own use." Aldave, *Misappropriation: A General Theory of Liability for Trading on Nonpublic Information*, 13 Hofstra L. Rev. 101, 116, 119 (1984). This sort of fraud is often put in terms of breach of a duty of disclosure; one party to a relationship of trust is entitled to rely on the loyalty of the other party unless the second party reveals an adverse interest. See generally Restatement (Second) of Agency §§ 389, 390, 395 comment c (1958). In such a situation, as Professor Keeton has explained, "the operative effect of nondisclosure, where the courts have imposed a duty to speak, is the same as if there had been a misrepresentation." Keeton, *supra*, 15 Tex. L. Rev. at 1-2. This duty to disclose need not be expressly imposed by the principal, as petitioners seem to assert (Pet. Br. 33, 34) (although the Journal did in fact expressly impose a disclosure obligation on Winans, as we explain at page 26, *infra*). It arises from the relationship of trust; a party to such a relationship is obligated to communicate to the other party "matters known to him that the other *is entitled* to know because of a fiduciary or other similar relation of trust and confidence between them." Restatement (Second) of Torts § 551(2)(a) (emphasis added). Cf. *Dirks* v. *SEC*, 463 U.S. 646, 655 n.14 (1983). While petitioners argue that it would have been anomalous to expect Winans to disclose his activities to the Journal, that fact demonstrates only that Winans' conduct was utterly inconsistent with the Journal's interests. See also Restatement (Second) of Torts §§ 529, 551(2)(b); Keeton, *supra*, 45 Tex. L. Rev. at 1, 6, 27; 2 F. Harper, F. James & O. Gray, *supra*, § 7.14, at 472, 474.

b. Contrary to petitioners' contention (Pet. Br. 33-36), a relationship of trust, in which concealment and nondisclosure of a breach of duty may disadvantage the victim, does not depend on the existence of a formally denominated "fiduciary" duty: it has long been understood that "[t]he confidential relationship is not at all confined to any specific association of the parties to it." *Appeal of Darlington*, 147 Pa. 624, 629-630, 23 A. 1046, 1047 (1892). Such associations include not only formal trust relationships, but also those of "principal and agent, master and servant, * * * and, generally, all persons who are associated by any relation of trust and confidence" (*ibid.*). See Restatement (Second) of Torts § 551 comment e; Restatement (Second) of Agency §§ 381, 389 (1958); 2 F. Harper, F. James & O. Gray, *supra*, § 7.14, at 473-474 & n.11.

As the common law recognizes, the relationship of employer and employee has these characteristics of trust and confidence. An employee has a duty not only to work loyally for the benefit of his employer, but also to disclose matters relevant to his employment and to refrain from acting in a manner adverse to his employer's interests absent full disclosure to the employer. See Restatement (Second) of Agency §§ 381, 389, 390 and comment d, 395.[13] It follows that an employee, no less than

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[13] Agents generally are "subject to a duty" to give to their principals "information which is relevant to the affairs entrusted to [them] and which, as the agent[s] ha[ve] notice, the principal[s] would desire to have." Restatement (Second) of Agency § 381. An agent must disclose such information "although not specifically instructed to do so. The duty exists if the agent has notice of facts which, in view of his relations with the principal, he should know may affect the desires of the principal as to his own conduct." *Id.* § 381 comment a. In addition, the common law rule is that "an agent is subject to a duty to the principal not to use or communicate information confidentially given him by the principal or acquired by him during the course of or on account of his agency * * * to the injury of the principal, on his own account or on behalf of another." *Id.* § 395. This rule precludes the use by the agent of confidential information "for any purpose likely to cause his principal harm * * *. Thus, an agent who is told by the prin-

anyone else in a relationship of confidence grounded in mutual understandings, engages in the special form of dishonesty and deception that accompanies a breach of trust when he "hold[s] himself out to be a loyal employee, acting in [the employer's] best interests, but actually not giving his honest and faithful services, to [the employer's] real detriment." *United States* v. *Bryza*, 522 F.2d 414, 422 (7th Cir. 1975), cert. denied, 426 U.S. 912 (1976). Such an employee, "in using [his] relationship [of trust and confidence with his employer] for the express purpose of carrying out a scheme to obtain his employer's confidential information and other property * * * would be guilty of deliberately producing a false impression on his employer in order to cheat him. Such conduct would constitute a positive fraud." *United States* v. *Procter & Gamble Co.*, 47 F. Supp. 676, 678 (D. Mass. 1942).[14]

The courts of appeals have thus uniformly held, in Judge Friendly's words, that "a scheme to use a private fiduciary position to obtain direct pecuniary gain is within the mail fraud statute," at least where that scheme contemplates some sort of harm to the principal. *United States* v. *Dixon*, 536 F.2d 1388, 1399-1400 (2d Cir. 1976). Without dissent on the point,[15] the courts of

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cipal of his plans * * * is not privileged to use such information at his principal's expense." *Id.* § 395 comment a.

[14] Use of a continuing misimpression to gain access to property or information is even more obviously a crime of "trick, deceit, chicane, or overreaching" than offenses such as embezzlement or misappropriation, which are understood to be " 'garden variety' type[s] of fraud" (*Superintendent of Insurance* v. *Bankers Life & Casualty Co.*, 404 U.S. 6, 11 n.7 (1971)); embezzlement need involve no more than a betrayal of confidence by the defendant *after* he has been entrusted with the victim's property. See *Grin* v. *Shine*, 187 U.S. 181, 189-190 (1902) ("it is impossible for a person to embezzle the money of another without committing a fraud upon him"); *Parr* v. *United States*, 363 U.S. 370, 385 (1960). See generally 2 W. LaFave & A. Scott, *Substantive Criminal Law* § 8.6 (1986).

[15] Petitioners have cited a number of opinions (primarily dissents and separate concurrences) and law review articles for the

appeals have concluded, as the District of Columbia Circuit explained in a thoughtful opinion, that "[s]o long as the jury finds [that the employee's] non-disclosure furthers a scheme to abuse the trust of the employer in a manner that makes an identifiable harm to him, apart from the breach itself, reasonably foreseeable, it may convict the employee of fraud." *Lemire*, 720 F.2d at 1337.[16] And the courts of appeals have reached what has

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general proposition that "expansion of the mail and wire fraud statutes have been severely criticized" (Pet. Br. 28; see *id.* at 28 n.56, 29 n.57, 29-30 n.58). Whatever the validity of that criticism, however, it has been leveled almost entirely at aspects of mail and wire fraud doctrine that are not at issue in this case. See, *e.g.*, *United States* v. *Weiss*, 752 F.2d 777, 791 (2d Cir.) (Newman, J., dissenting) (addressing specificity of the indictment), cert. denied, No. 84-1645 (Nov. 4, 1985); *United States* v. *Margiotta*, 688 F.2d 108, 140 (2d Cir. 1982) (Winter, J., dissenting) (addressing application to political party officials), cert. denied, 461 U.S. 913 (1983); *United States* v. *Craig*, 573 F.2d 455, 497 (7th Cir. 1977) (Swygert, J., dissenting) (addressing use of mails on the facts of that case), cert. denied, 439 U.S. 820 (1978); Jeffries, *Legality, Vagueness, and the Construction of Penal Statutes*, 71 Va. L. Rev. 189, 237-242 (1985) (addressing application to political party officials). And *none* of the decisions cited by petitioners has taken issue with the fundamental (and here dispositive) proposition that an employee may commit a fraud by obtaining a benefit, at his employer's expense, by abusing the employer's misplaced trust. While a number of the opinions and articles cited by petitioners suggest that the deprivation of an employee's loyal services, standing alone, cannot support a prosecution under Sections 1341 and 1343, that conclusion, even if correct, is simply inapposite in this case: the government charged, and both courts below found, that the victim here suffered *other* substantial and expectable injuries. See pages 28-32, *infra*.

[16] See, *e.g.*, *United States* v. *Conner*, 752 F.2d 566, 572 (11th Cir.), cert. denied, 474 U.S. 821 (1985); *United States* v. *Alexander*, 741 F.2d 962 (7th Cir. 1984); *United States* v. *Siegel*, 717 F.2d 9, 13-14 (2d Cir. 1983); *United States* v. *Feldman*, 711 F.2d 758, 763 (7th Cir.), cert. denied, 464 U.S. 939 (1983); *United States* v. *Curry*, 681 F.2d 406, 409, 411 (5th Cir. 1982); *United States* v. *Ballard*, 663 F.2d 534, 540 (1981) (dictum), modified on reh'g, 680 F.2d 352 (5th Cir. 1982); *United States* v. *Bronston*, 650 F.2d 920, 926 (2d Cir. 1981), cert. denied, 456 U.S. 915 (1982); *United States* v. *Shamy*, 656 F.2d 951, 957 (4th Cir.

been called a "judicial consensus" that the duty giving rise to the fraud may stem from an employment relationship. *Id.* at 1335-1336.[17]

c. The concept of fraud is in fact substantially broader than necessary to sustain the conviction here, and petitioners are simply wrong in arguing (see Pet. Br. 31, 36) that there is some novelty in treating a breach of trust or fiduciary duty as either fraudulent or criminal. At the time of the enactment of the original predecessor to Section 1341 in 1872, a breach of duty by one with whom the victim shared "any relation of trust and confidence" (*Darlington*, 147 Pa. at 629-630, 23 A. at 1047) was well understood to be fraudulent.[18] This

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1981), cert. denied, 455 U.S. 939 (1982); *United States* v. *Von Barta*, 635 F.2d at 1007; *United States* v. *Bohonus*, 628 F.2d 1167, 1172 (9th Cir.), cert. denied, 447 U.S. 928 (1980); *United States* v. *Reece*, 614 F.2d 1259, 1261 (10th Cir. 1980); *United States* v. *Bryza*, 522 F.2d 414, 422 (7th Cir. 1975), cert. denied, 426 U.S. 912 (1976); *Post*, 407 F.2d at 329. Cf. *Abbott* v. *United States*, 239 F.2d 310, 314 (5th Cir. 1956). In addition, the courts of appeals have uniformly held that a public official commits fraud when he corruptly breaches his duties to the public. See, *e.g.*, *United States* v. *Silvano*, 812 F.2d 754, 758-759 (1st Cir. 1987); *United States* v. *Lovett*, 811 F.2d 979 (7th Cir. 1987); *United States* v. *Margiotta*, 688 F.2d 108, 120 (2d Cir. 1982), cert. denied, 461 U.S. 913 (1983); *United States* v. *Mandel*, 591 F.2d 1347, 1357-1364, aff'd in relevant part, 602 F.2d 653 (4th Cir. 1979) (en banc), cert. denied, 445 U.S. 961 (1980); *United States* v. *Isaacs*, 493 F.2d 1124, 1149 (7th Cir.), cert. denied, 417 U.S. 976 (1974); *United States* v. *States*, 488 F.2d 761, 763-767 (8th Cir. 1973), cert. denied, 417 U.S. 909 (1974); *United States* v. *Edwards*, 458 F.2d 875, 880-881 (5th Cir.), cert. denied, 409 U.S. 891 (1972). For earlier cases involving both public and private fiduciaries, see page 26 and note 23, *infra*.

[17] See, *e.g.*, *United States* v. *Conner*, 752 F.2d 566, 572 (11th Cir. 1985), cert. denied, 474 U.S. 821 (1985); *United States* v. *Ballard*, 663 F.2d at 541; *United States* v. *Von Barta*, 635 F.2d at 1007; *United States* v. *Reece*, 614 F.2d at 1261; *United States* v. *Bryza*, 522 F.2d at 422.

[18] The relation of principal and agent in particular was understood at the time to be one of trust and confidence. See, *e.g.*, M. Bigelow, *The Law of Fraud* 222 (1877); T. Cooley, *A Treatise*

Court regularly noted in the nineteenth century that self-dealing agents or trustees "commit[ted] * * * fraud upon" their principals. *Wardell* v. *Railroad Co.*, 103 U.S. 651, 657 (1880). See, *e.g.*, *Michoud* v. *Girod*, 45 U.S. (4 How.) 503, 553 (1846). Indeed, courts of equity in the nineteenth century recognized as frauds " 'all acts, omissions and concealments which involve a breach of legal or equitable duty, trust, or confidence, justly reposed, and are injurious to another.' " *Moore* v. *Crawford*, 130 U.S. 122, 128 (1889) (quoting 1 J. Story, *Equity Jurisprudence* § 187). See *Capital Gains Research Bureau*, 375 U.S. at 143-144; *United States* v. *Carter*, 217 U.S. 286, 306 (1910).[19]

Congress plainly had these general notions of fraud in mind when it enacted Section 1341. While the legislative history of the statute is not illuminating,[20] Congress's choice of language expressed an extraordinarily broad purpose. The statute's "any scheme or artifice to

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on the Law of Torts 595 (2d ed. 1888); F. Tiffany, *Handbook of the Law of Principal and Agent* 415 (1903).

[19] The rationale for this principle was plain: in cases where the interests of a principal and agent are adverse, "[t]he employers are, thus, thrown off their guard; they are led to suppose they have an agent acting solely with a view toward their interest * * * while, in fact, the agent is conferring with himself." 1 J. Hovenden, *A General Treatise on the Principles and Practice by Which the Courts of Equity are Guided as to the Prevention or Remedial Correction of Fraud* 145 (1832).

[20] Virtually the only legislative history of the 1872 legislation—which, like the current version of the mail fraud statute, prohibited "any scheme or artifice to defraud"—is the statement by one of the sponsors that the act was directed at "frauds which are mostly gotten up in large cities * * * by thieves, forgers, and rapscallions generally, for the purposes of deceiving and fleecing the innocent people in the country." Cong. Globe, 41st Cong., 3d Sess. 35 (1870) (remarks of Rep. Farnsworth). Although the statute has since been amended on several occasions, none of the modifications has affected (or has shed light on the meaning of) the "scheme or artifice to defraud" language. See generally Rakoff, *The Federal Mail Fraud Statute (Part I)*, 18 Duq. L. Rev. 771, 779-780 (1980).

defraud" formula was novel; that phrase's general reference to "fraud"—a term that was understood at the time to encompass breaches of trust—omitted familiar limitations found both in the ancient property offenses such as false pretenses and in the common law civil action of deceit.[21] As a result, this Court and the lower federal courts, from the time of their earliest interpretations of the mail fraud statute, made it clear

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[21] Compare 1 J. Bishop, *Commentaries on the Criminal Law* §§ 565-590 (7th ed. 1882) (setting out technical requirements for property crimes such as embezzlement and false pretenses); 2 W. LaFave & A. Scott, *Substantive Criminal Law* 327-409 (1986) (same); Pearce, *Theft by False Promises*, 101 U. Pa. L. Rev. 967 (1953) (same); T. Cooley, *A Treatise on the Law of Torts* 555-556 (2d ed. 1888) (setting out requirements for common law action of deceit). Indeed, decisions and treatises of the time referred to the common law action for misrepresentation not as "fraud" but as "deceit." See, *e.g.*, J. Bishop, *Commentaries on the Non-Contract Law* 132-144 (1889); T. Cooley, *supra*, at 555-556; 1 E. Jaggard, *Hand-Book of the Law of Torts* 558-602 (1895); F. Pollock, *A Treatise on the Law of Torts* 348-388 (1894). In contrast, the term "fraud," when used alone, signified a range of overreaching conduct, including both misrepresentation and breach of trust. See 1 J. Hovenden, *supra*, at 145-177; M. Bigelow, *The Law of Fraud* (1877); T. Cooley, *supra*, at 554-555, 595-621; 2 F. Hilliard, *The Law of Torts* 74 (1874). See also 1 *Bouvier's Law Dictionary* 530 (1897) ("[t]o defraud is to withhold from another that which is justly due him, or to deprive him of a right by deception and artifice"; W. Anderson, *A Dictionary of Law* 474 (1893); 2 J. Stephen, *A History of the Criminal Law of England* 121 (1883) (hallmark of fraud is "deceit or intention to deceive or in some cases mere secrecy"). Because fiduciary self-dealing was presumed to involve overreaching, such breaches of duty were often labeled "constructive frauds" and were treated as improper even where the trustee acted in good faith. See generally 1 J. Hovenden, *supra*, at 145-177; M. Bigelow, *supra*, at 190-318. Where the fiduciary acted with an intention to take advantage of his position of trust, however, his actions were understood to be not only "constructively" but "actually" improper. See M. Bigelow, *supra*, at lviii (1877) ("In all cases of constructive fraud, there may also be actual fraud."). The term "fraud," when understood to signify a dishonest intent, was seen as "one of the elements of [the] specific tort called Deceit." M. Bigelow, *Elements of the Law of Torts* 16 (7th ed. 1901).

that Section 1341 reaches beyond both the crime of false pretenses and common law misrepresentation. *Durland* v. *United States*, 161 U.S. 306, 313 (1896); *United States* v. *Loring*, 91 F. 881 (N.D. Ill. 1884); *United States* v. *Bernard*, 84 F. 634 (C.C.S.D.N.Y. 1898); *O'Hara* v. *United States*, 129 F. 551 (6th Cir. 1904). See generally Rakoff, *The Federal Mail Fraud Statute (Part I)*, 18 Duq. L. Rev. 771, 799 (1980); Note, *Survey of the Law of Mail Fraud*, 1975 Ill. L.F. 237-239. Indeed, the Court consistently held that the predecessor to 18 U.S.C. 371, a companion statute to Section 1341 that makes it illegal to conspire to "defraud the United States * * * in any manner," reaches corruption and breach of duty on the part of public officials even in the absence of any affirmative misstatement on their part.[22]

Given this background, it is not surprising that the courts of appeals, from the time of their first encounter with the issue, have held that breaches of duty by employees or other persons in positions of trust and confidence—either private or public—violate the mail fraud statute. Almost 50 years ago, the Second Circuit upheld a prosecution under the predecessor to Section 1341 on the theory that "[u]sing a fiduciary position as a [bondholder] protective committee member to obtain secret profits based upon inside information is not only a breach of trust, but an active fraud on the bondholders." *United States* v. *Buckner*, 108 F.2d 921, 926 (2d Cir.), cert. denied, 309 U.S. 669 (1940). And other courts of

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[22] See *Haas* v. *Henkel*, 216 U.S. 462, 476-477 (1910); *Glasser* v. *United States*, 315 U.S. 60, 66 (1942); Coffee, *From Tort to Crime: Some Reflections on the Criminalization of Fiduciary Breaches and the Problematic Line Between Law and Ethics*, 19 Am. Crim. L. Rev. 117, 123 n.32 (1981). Originally enacted in 1867 (Act of Mar. 2, 1867, ch. 169, § 30, 14 Stat. 484), Section 371 was understood even before the passage of Section 1341 to be "more comprehensive" than the common law. *United States* v. *Whalan*, 28 F. Cas. 531, 532 (D. Mass. 1868) (No. 16609).

appeals uniformly came to the same conclusion in the immediately succeeding years.[23]

d. Petitioners' conduct involved a deliberate and deceptive breach of Winans' duty of trust. Winans plainly occupied a position of trust and confidence at the Journal. Winans knew that he had been entrusted with the Journal's most sensitive and confidential information—some of which he was hired to create for the Journal's benefit—and that the Journal considered the information strictly "the Company's property" (J.A. 41-42). He knew that his employer considered it "essential" (*id.* at 41, 43) that he not disclose that information or use it to buy and sell securities on his own account. He was specifically told (*id.* at 41), and was found by the district court to have understood (Pet. App. 37a), that compliance with the Journal's conflict rules was a condition of his continued employment. He was given special and repeated reminders of the importance of confidentiality (*id.* at 36a). The Journal thus plainly expected Winans not to use, and to report any unauthorized use of, its confidential information. And

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[23] *Shushan*, 117 F.2d at 115. See *United States* v. *Groves*, 122 F.2d 87, 90 (2d Cir.), cert. denied, 314 U.S. 670 (1941); *Bradford* v. *United States*, 129 F.2d 274, 275 (5th Cir.), cert. denied, 317 U.S. 683 (1942); *Steiner* v. *United States*, 134 F.2d 931, 933 (5th Cir.), cert. denied, 319 U.S. 774 (1943); *United States* v. *Classic*, 35 F. Supp. 457, 458 (D. La. 1940), aff'd on other grounds, 313 U.S. 299 (1941). See generally *Epstein* v. *United States*, 174 F.2d 754, 766-768 (6th Cir. 1949); *Procter & Gamble Co.*, 47 F. Supp. at 678. These cases have a special significance for the interpretation of the wire fraud statute, Section 1343. That statute, which is obviously modeled on Section 1341, was enacted in 1952. Communications Act Amendments, ch. 879, § 18(a), 66 Stat. 722. While the legislative history of Section 1343 is not extensive (see S. Rep. 44, 82d Cong., 1st Sess. 14 (1951)), Congress passed the wire fraud statute against the background of the series of successful breach of trust prosecutions under Section 1341, including a number of prosecutions involving public officials and prominent private parties. The drafters of Section 1343 can be presumed to have been familiar with this use of Section 1341—which had been repeatedly affirmed by the courts of appeals—and to have endorsed it when they borrowed the language of Section

contrary to petitioners' assertion (Pet. Br. 33, 34 & n.77), this latter duty of disclosure arose not only from Winans' common law duty as an employee but from his employer's explicit requirements: the district court specifically found that "it was part of [Winans'] job" to "tell his editors if he heard that word was out about a column's topic" (Pet. App. 37a).[24]

Winans' conceded violation of these duties was not, as petitioners like to suggest, merely a breach of his employer's workrules and a failure to tell about it. The success of petitioners' scheme depended on Winans' continuing, fictitious *pose* as a loyal employee. Petitioners *used* the Journal's misimpression that Winans was a loyal employee who was complying with his employer's rules to gain access to a flow of confidential information. That flow of information would not have started in the absence of Winans' at least implicit representations of loyalty; it would not have continued had Winans disabused the Journal of its mistaken belief in the continuing validity of those representations, or had he complied with his specific duty to disclose leaks of the *Heard* column.

Winans thus did more than simply break the Journal's rules or deprive the Journal of his own loyalty: he took advantage of what he knew to be the Journal's misimpression of his motives and actions to remain in a position that allowed him access to the Journal's property—confidential information—for use in a scheme that threatened an independent harm to the Journal. The

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1341 in writing the wire fraud statute. See, *e.g.*, *Herman & Maclean* v. *Huddleston*, 459 U.S. 375, 385-386 (1983); *Merrill Lynch, Pierce, Fenner & Smith* v. *Curran*, 456 U.S. 353, 381-382 (1982); *Lorillard* v. *Pons*, 434 U.S. 575, 580-581 (1978).

[24] Petitioners suggest (Pet. Br. 34 n.77) that Winans was not obligated to comply with this requirement because he himself was the one responsible for the improper disclosure of the information. But it is hardly likely that Winans' simultaneous violation of *two* duties—his improper use of confidential information and his failure to disclose the misuse of that information—insulates him from liability for both violations.

district court thus found that Winans and Felis (aided by Carpenter) acted with a specific intent to defraud the Journal (Pet. App. 72a), which included a "'specific intent to deceive'" (*id.* at 67a (citation omitted)). And the court properly concluded as well that the scheme did in fact operate as a "deceit on the Wall Street Journal" (*id.* at 71a). Such a scheme, which was possible only because the Journal relied on Winans' good faith, and which could continue only because petitioners concealed Winans' abuse of his position, was a fraud.

e. The holdings below do not, as petitioners portentously assert, convert "disobedience of any internal workrule" into "a mail or wire fraud violation, no matter how technical the rule or trivial the conduct it prohibits" (Pet. Br. 34-35).[25] This case involves deception (in the sense of a deliberate failure by one party in a relationship of trust and confidence to correct a misimpression held by the other party); it involves the use of that misimpression to obtain access, on a continuing basis, to the employer's property (here, confidential information); and it involves use of that property in a manner that not only violated the employer's rules but involved a harm to the employer independent of the employer's loss of the employee's loyal services. Courts and commentators, including those cited with approval by petitioners, have recognized that circumstances such as these demonstrate deceitful conduct that is appropriately

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[25] The misconduct here was hardly trivial. Compliance with the Dow Jones rules breached by Winans was understood to be important to the preservation of the Journal's reputation. While petitioners assert (Pet. Br. 6, 35 & n.81) that most newspapers do not have rules like the Journal's, the single newspaper story upon which petitioners rely for this surprising proposition was not admitted into evidence on the point by the district judge (see Gov't C.A. Br. 63 n.**); the government pointed to other accounts indicating that most newspapers and magazines do in fact have a policy similar to that of Dow Jones. Indeed, even the article upon which petitioners rely indicates that newspapers that lack such a formal policy nevertheless expect their employees not to trade on confidential pre-publication information.

treated as criminal under a properly cabined interpretation of the mail and wire fraud statutes. See, *e.g.*, *Lemire*, 720 F.2d at 1336-1338 (cited at Pet. Br. 29 n.57); Coffee, *supra*, 19 Am. Crim L. Rev. at 134, 167 (cited at Pet. Br. 29 n.58, 37); *id.* at 122-123 n.30 (citing cases). Indeed, as we demonstrate below, petitioners' scheme was sufficiently elaborate to require use of the mails and interstate wires for its success, a factor that is hardly likely to be true in cases involving trivial or offhand infractions of workrules.[26]

2. *Harm to the victim.* a. In addition to an element of trickery and violation of trust, it is common ground that, for a course of conduct to be prosecuted as a "scheme or artifice to defraud," it must pose a risk of harm to the victim. In this case, as both courts below explained, that requirement was amply satisfied by the danger petitioners knowingly posed to the Journal's reputation.[27] While petitioners complain that actual harm to the Journal was not established at trial (Pet. Br. 41), they acknowledge (*ibid.*)—as the courts have uniformly held—that proof of injury-in-fact is not necessary under Sections 1341 and 1343, so long as the scheme contemplated or created a risk of harm.[28] Here, both the district court and the

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[26] Petitioners' other complaints—that the Journal's rules were imposed unilaterally (Pet. Br. 33), that the decisions below give "every employer the power to decide what acts are indictable as felonies" (*id.* at 36), and that the approach taken by the lower courts creates a federal law of fiduciary obligations (*ibid.*)—are rhetorical exercises rather than substantial arguments. Petitioners were prosecuted not for traversing a work rule, but for a scheme that induced the Journal to give them access to information that they used to its detriment. See also notes 12, 13, *supra*.

[27] Injury to the Journal need not have been a goal of the scheme so long as it was a likely consequence of petitioners' activities. See 2 J. Stephen, *supra*, at 121-122.

[28] See, *e.g.*, *United States* v. *Louderman*, 576 F.2d 1383, 1387 (9th Cir.), cert. denied, 439 U.S. 896 (1978); *United States* v. *Reid*, 533 F.2d 1255, 1261 & n.24 (D.C. Cir. 1976) (citing cases); *United States* v. *Lowe*, 115 F.2d 596, 597 (7th Cir.), cert. denied, 311 U.S. 717 (1940). See generally Coffee, *supra*, 19 Am. Crim. L. Rev. at 127. The courts have reached this conclusion because Sections 1341 and 1343 make the "scheme" itself criminal, once a

court of appeals found that petitioners' scheme raised the prospect of "potentially devastating harm" to the Journal (Pet. App. 65a; see *id.* at 18a, 24a). Petitioners' argument (Pet. Br. 41) that their actions did not really put the Journal's reputation at risk is a mere quarrel with these concurrent findings of fact.

These findings by the courts below are plainly correct. The Journal itself had concluded that the misuse of its confidential information by an employee could result in "tremendous embarrassment and damage to the Company's reputation" (J.A. 41); Dow Jones adopted its rules to forestall precisely that eventuality. And petitioners' argument to the contrary sounds a particularly sour note here when placed against the district court's specific finding that "[t]he scheme's injurious consequences to the Journal must have been known to Winans" (Pet. App. 64a) and to the other participants (*id.* at 64a-65a).

b. Citing the common law of deceit and this Court's decisions in *Fasulo* v. *United States*, 272 U.S. 620 (1926), and *Hammerschmidt* v. *United States*, 265 U.S. 182 (1924), petitioners also make the broader argument (Pet. Br. 38-39 & n.95, 41 n.106) that a scheme is "fraudulent" only if it deprives the victim of money or tangible property. Whatever the limitations on the common law tort of deceit, however, this Court and the lower federal courts settled almost 100 years ago that Congress intended Section 1341 to reach beyond both the common law and other property crimes. See pages 23-24, *supra*. And *Fasulo* did not, as petitioners assert, "insist[ ] on tangible economic injury" in a prosecution

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mailing or wiring in furtherance of the fraud has taken place. Petitioners disregard this point in asserting that "the prosecution was unable to firmly establish that Winans' breaches caused any harm, economic or otherwise, to the Journal" (Pet. Br. 41 (footnote omitted)). In fact, as the district court noted (Pet. App. 63a-64a), the government introduced considerable evidence to establish that the Journal had suffered an injury; the court made no findings on the point because it found it sufficient that the scheme contemplated harm to the Journal (*id.* at 64a-65a).

under Section 1341 (Pet. Br. 41 (footnote omitted)); to the contrary, the Court there indicated in general terms that "fraud" involves "the deprivation of something of value" (272 U.S. at 627), a conclusion that reflected the understanding of the word at the time of the enactment of the mail fraud statute.[29]

Similarly, *Hammerschmidt*, far from confining "fraud" to schemes to take money or tangible property, explicitly recognized—as the Court had before (see *Haas v. Henkel*, 216 U.S. 462, 479-480 (1910)) and has since (see *United States* v. *Johnson*, 383 U.S. 169, 172 (1966))—that a conspiracy to defraud the United States under 18 U.S.C. 371 may include a scheme to "interfere with or obstruct one of [the United States'] lawful government functions" (265 U.S. at 188). And the courts of appeals have since held without exception under Sections 1341 and 1343 that "criminal fraud encompasses schemes to defraud persons of significant intangibles" (*Lemire*, 720 F.2d at 1336).[30] Indeed, a contrary conclusion would be

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[29] Legal dictionaries of the late nineteenth century, for example, defined "defraud" as meaning, among other things, "[t]o withhold from another what is justly due him, or to deprive him of a right, by deception or artifice" (W. Anderson, *supra*, at 474); the term "right" was in turn defined as "an enforceable claim or title to any subject matter whatever: either to possess or enjoy a tangible thing, or to do some act, pursue a course, enjoy a means of happiness, or to be exempt from any cause of annoyance" (*id.* at 905). See 1 *Bouvier*, *supra*, at 927. See also 2 J. Stephen, *A History of the Criminal Law of England* 121-122 (1883) (fraud involves "injury" to another).

[30] See, *e.g.*, *United States* v. *Alexander*, 741 F.2d 962 (7th Cir. 1984); *United States* v. *Frankel*, 721 F.2d 917, 920 (3d Cir. 1983) (dictum); *United States* v. *Boffa*, 688 F.2d 919, 925 (3d Cir. 1982) (citing cases), cert. denied, 460 U.S. 1022 (1983); *United States* v. *Curry*, 681 F.2d 406, 410-411 (5th Cir. 1982) (dictum); *United States* v. *Ballard*, 663 F.2d 534, 540 (1981) (dictum), modified on *reh'g*, 680 F.2d 352 (5th Cir. 1982); *United States* v. *Bohonus*, 628 F.2d 1167, 1171 (9th Cir.), cert. denied, 447 U.S. 928 (1980); *United States* v. *Reece*, 614 F.2d at 1261; *United States* v. *Condolon*, 600 F.2d 7, 8-9 (4th Cir. 1979); *United States* v. *Louderman*, 576 F.2d at 1387; *United States* v. *Castor*, 558 F.2d 379, 383 (7th Cir. 1977), cert. denied, 434 U.S. 1010 (1978); *United States*

remarkable given the realities of the modern world, where intangible interests such as information, business opportunities, goodwill, and contract rights have enormous value.

The Journal's reputation for reliability and integrity, moreover, was a concrete, pre-existing asset, independent of the Journal's interest in Winans' loyal services. Petitioners themselves recognized this, for they used that asset in their scheme: the Journal's reputation gave the *Heard* column the market punch that allowed petitioners to reap their " 'no-risk profits.' " [31] Indeed, as principles of libel and defamation law make clear, reputation—

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v. *Bryza*, 522 F.2d at 421-422. In a series of other decisions, the courts similarly have held that the corruption of a public official defrauds the citizenry by depriving it of the loyal services of the official. See, *e.g.*, *United States* v. *Silvano*, 812 F.2d 754, 758-759 (1st Cir. 1987); *United States* v. *Lovett*, 811 F.2d 979 (7th Cir. 1987); *United States* v. *Margiotta*, 688 F.2d 108 (2d Cir. 1982), cert. denied, 461 U.S. 913 (1983); *United States* v. *Mandel*, 591 F.2d 1347, 1357-1364 (4th Cir. 1979), aff'd in relevant part, 602 F.2d 653 (en banc), cert. denied, 445 U.S. 961 (1980); *United States* v. *Rabbitt*, 583 F.2d 1014, 1026 (8th Cir. 1978), cert. denied, 439 U.S. 1116 (1979); *United States* v. *Brown*, 540 F.2d 364, 374 (10th Cir. 1976); *Dixon*, 536 F.2d at 1400 (Friendly, J.) (dictum); *United States* v. *Keane*, 522 F.2d 534, 546 (7th Cir. 1975), cert. denied, 424 U.S. 976 (1976); *United States* v. *Isaacs*, 493 F.2d 1124, 1149-1150 (7th Cir.), cert. denied, 417 U.S. 976 (1974); *United States* v. *States*, 488 F.2d 761, 766 (8th Cir. 1973), cert. denied, 417 U.S. 909 (1974); *United States* v. *Edwards*, 458 F.2d 875, 880-881 (5th Cir.), cert. denied, 409 U.S. 891 (1972); *Bradford* v. *United States*, 129 F.2d 274, 276 (5th Cir.), cert. denied, 317 U.S. 683 (1942). Whether the deprivation of a public official's loyal services may support a conviction under the mail and wire fraud statutes currently is before the Court in *McNally* v. *United States*, No. 86-234, and *Gray* v. *United States*, No. 86-286.

[31] Petitioners appear to suggest (Pet. Br. 41) that the Court rejected reputation as an interest protected by the mail fraud statute when it indicated in *Fasulo* that a blackmail threat sent through the mails does not amount to a scheme to defraud. In fact, however, the Court merely suggested in that case that the scheme involved a simple threat rather than trickery or deceit; the significance of potential injury to reputation was never addressed. See 272 U.S. at 628-629.

unlike certain other interests whose deprivation also has been held to create liability under the mail and wire fraud statutes[32]—is "recognized in law as having independent value" (*Lemire*, 720 F.2d at 1336-1337 n.11). See, *e.g.*, *Gertz* v. *Robert Welch, Inc.*, 418 U.S. 323, 341 (1974). That is particularly true where the injury is suffered by a financial newspaper, which is able to gather information and maintain its readership precisely because of its reputation for reliability and integrity. The district court accordingly concluded that the Journal's reputation is "probably its most valuable asset" (Pet. App. 64a). By scheming to put that asset at risk, petitioners defrauded the Journal " 'as surely as if they took [its] money' " (*id.* at 18a (citation omitted)).

3. *Mailings and Wirings.* Petitioners finally argue that they did not, in the language of Sections 1341 and 1343, "cause" the mailings and wirings in this case—the wiring of Winans' column to the Journal's printing plant and the mailing of the Journal to its subscribers—"for the purpose of executing" their scheme. As they elliptically acknowledge, however, they did in fact "cause" the mailings and wirings as a matter of "general proximate causality" (Pet. Br. 45). And that concession is compelled by this Court's decisions. "Where one does an act with knowledge that use of the mails will follow in the ordinary course of business, or where such use can reasonably be foreseen * * * then he 'causes' the mails to be used." *Pereira* v. *United States*,

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[32] As we note above (note 30, *supra*), for example, the courts of appeals have held that the fraudulent deprivation of an employee's loyal and honest services will support a conviction under the mail and wire fraud statutes. Petitioners attack these holdings with particular vigor (see Pet. Br. 39, 40). But petitioners' argument on this point, whatever its merits as a theoretical matter, is simply irrelevant here. Contrary to petitioners' assertion, the harm alleged by the government and found by both courts below was the threat posed by the scheme to the Journal's reputation, not the loss of Winans' loyal services (although it is manifest, of course, that the scheme did in fact deprive the Journal of Winans' loyalty).

347 U.S. 1, 8-9 (1954) (citation omitted). Here, Winans did just that by producing his columns and delivering them to his editors with the expectation that they would be wired to the Journal's printing plant and mailed to the Journal's subscribers.

These mailings and wirings, moreover, were essential to the scheme. As the district court explained, "[t]his is hardly a situation where the nexus between the mailings and wirings and the alleged fraud is too remote; without publication and distribution of the copies of the Journal containing the columns in question there would be no point to the scheme" (Pet. App. 66a (footnote omitted)). Petitioners' suggestion (Pet. Br. 43) that the mailings and wirings were "irrelevant" to their trading is for that reason wholly incorrect. Petitioners' further observations that the mailings were not directed to the victim of the fraud and that those mailings may have occurred after Winans leaked the Journal's confidential information (*id.* at 44) are simply beside the point. See, *e.g.*, *Pereira*, 347 U.S. at 4-6, 8; *United States* v. *Sampson*, 371 U.S. 75, 80-81 (1962). It is enough that the mailings and wirings were "incident to an essential element of the scheme" (*Pereira*, 347 U.S. at 8-9). And the mailings and wirings here were clearly that. See generally *United States* v. *Muni*, 668 F.2d 87, 89 (2d Cir. 1981); *United States* v. *Castor*, 558 F.2d 379, 385 (7th Cir. 1977), cert. denied, 434 U.S. 1010 (1979); *Gregory* v. *United States*, 253 F.2d 104, 109 (5th Cir. 1958). Cf. *United States* v. *Green*, 786 F.2d 247, 250 (7th Cir. 1986).

Petitioners' principal contention is that they did not cause the mailings here "for the purpose" of executing their scheme, because, they assert (a) the timing and accuracy of Winans' columns were not affected by the fraud, and (b) the columns accordingly would have been mailed and wired in the same form even in the absence of a fraud. But whatever the accuracy of these asser-

tions,[33] success of the scheme depended, as petitioners acknowledge, on "t[aking] advantage of the fact that Winans' columns would be printed and distributed" (Pet. Br. 44). Winans produced his columns, and introduced them onto the interstate wires and into the mails, with the fixed intention of using those columns (once transported) to commit a fraud. He is in no position to claim now that his use of the mails and wires in furtherance of that scheme was fortuitous, or that the arguable existence of a legitimate purpose for the mailings and wirings eliminates his manifestly fraudulent aims.[34]

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[33] Quite apart from the question whether Winans altered the timing or contents of specific columns to suit the scheme, as to which see note 4, *supra*, there is no reason to assume that the contents of the wirings and mailings would have been the same absent the scheme. Petitioners are not entitled to have Winans' profession as stock market profiteer treated as wholly incidental to his profession as journalist.

[34] Petitioners rely primarily on *Parr* v. *United States*, 363 U.S. 370 (1960) (Pet. Br. 45-46). In that case, however, the Court simply rejected the proposition that "mailings made under the imperative command of duty imposed by state law are criminal under the mail fraud statute" (363 U.S. at 391). See also *United States* v. *Curry*, 681 F.2d at 412; *United States* v. *Boyd*, 606 F.2d 792, 794 (8th Cir. 1979) (cited at Pet. Br. 46). See generally *United States* v. *Sampson*, 371 U.S. at 80. Winans, who produced his columns with the expectation of using them to commit a fraud, and who knew that his columns would not be published if he disclosed his breach of duty, plainly does not fall within this rule. The other cases relied upon by petitioners (see Pet. Br. 43 n.117, 45 n.120, 46) for the proposition that their actions failed to satisfy the mailing and wiring requirements of Sections 1341 and 1343 are simply inapposite. Those decisions held only that, on the particular facts involved, "there was not a sufficient connection between the mailing and the execution of the defendants' scheme." *United States* v. *Maze*, 414 U.S. 395, 401 (1974); *Kann* v. *United States*, 323 U.S. 88, 94 (1944); *United States* v. *Castile*, 795 F.2d 1273, 1278-1281 (6th Cir. 1986); *United States* v. *Taylor*, 789 F.2d 618, 622-623 (8th Cir. 1986); *United States* v. *Tarnopol*, 561 F.2d 466, 471-472 (3d Cir. 1977).

B. Petitioners' Trading In Securities On Fraudulently Acquired, Market-Affecting Information Violated Section 10(b) Of The Securities Exchange Act Of 1934 And Rule 10b-5 Thereunder

Petitioners used the information that they fraudulently misappropriated from the Journal to "'reap instant no-risk profits in the stock market'" (Pet. App. 19a-20a, quoting *SEC* v. *Materia*, 745 F.2d 197, 203 (2d Cir. 1984), cert. denied, 471 U.S. 1053 (1985)). Indeed, the purpose of their misappropriation was to take advantage of investors who "would not have purchased or sold, at least at the transaction prices, had they had the benefit of [the fraudulently acquired] information" (Pet. App. 18a). Petitioners nevertheless assert that, because the information that gave them this advantage was misappropriated from the Journal rather than from a "market participant" that was itself trading securities, their conduct was outside the "protective zone" (Pet. Br. 15) of Section 10(b), the Exchange Act's "catchall" anti-fraud provision. *Herman & Maclean* v. *Huddleston*, 459 U.S. 375, 382 (1983). See *Chiarella*, 445 U.S. at 226.

Petitioners' argument misconceives both the purpose and the theory of the prosecution here. Petitioners were prosecuted not to correct a private wrong, but to further the Exchange Act's fundamental purpose of "insur[ing] the maintenance of fair and honest markets in [securities] transactions." 15 U.S.C. 78b. And petitioners were not charged on the theory that they were "insiders" of the corporations whose stock they traded, who for that reason owed a duty of disclosure to the shareholders on the other side of their transactions. Petitioners were prosecuted and convicted on the theory that "misappropriation of confidential information by a fiduciary" for use in trading securities violates Section 10(b) and Rule 10b-5. *United States* v. *Newman*, 664 F.2d 12, 18 (2d Cir. 1981), aff'd after remand, 722 F.2d 729 (2d Cir.) (Table), cert. denied, 464 U.S. 863 (1983). The elimination of that sort of "cunning device" (*Ernst & Ernst* v. *Hochfelder*, 425 U.S. 185, 203 (1976) (brackets omit-

ted)) from trading is a central purpose of the securities laws.

1. Section 10(b) (emphasis added) makes it unlawful for "*any* person," "directly or indirectly," to use "in connection with the purchase or sale of *any* security * * * *any* manipulative or deceptive device or contrivance" in violation of rules promulgated by the SEC. Rule 10b-5 (emphasis added) in turn prohibits "*any* person" from engaging in "*any* act [or] practice" that "operates or would operate as a fraud or deceit upon *any* person" in connection with a purchase or sale of securities. This Court has consistently construed these provisions broadly, noting that Section 10(b) is "a 'catchall' clause to enable the Commission to 'deal with new manipulative or cunning devices'" (*Hochfelder*, 425 U.S. at 203 (brackets omitted)). The statute and rule thus "'prohibit *all* fraudulent schemes in connection with the purchase or sale of securities, whether the artifices employed involve a garden type variety of fraud, or present a unique form of deception.'" *Bankers Life*, 404 U.S. at 11 n.7 (quoting *A.T. Brod & Co.* v. *Perlow*, 375 F.2d 393, 397 (2d Cir. 1967) (emphasis in original)). See *Huddleston*, 459 U.S. at 386; *United States* v. *Naftalin*, 441 U.S. 768, 773 (1979); *Affiliated Ute Citizens* v. *United States*, 406 U.S. 128, 151 (1972). See also S. Rep. 792, 73d Cong., 2d Sess. 6 (1934).

Petitioners' fraudulent misappropriation and use of confidential information in breach of a duty of trust was a fraud on "any person"—The Wall Street Journal.[35]

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[35] In the report accompanying the Insider Trading Sanctions Act of 1984, Pub. L. No. 98-376, 98 Stat. 1264, the House explained that "[i]n other areas of the law, deceitful misappropriation of confidential information by a fiduciary * * * has consistently been held to be unlawful;" it added that Congress "has not sanctioned a less rigorous code of conduct under the federal securities laws." H.R. Rep. 98-355, 98th Cong., 1st Sess. 5 (1983). Indeed, the idea that misappropriation of confidential information constitutes a fraud has particular force in the securities area. See *Materia*, 745 F.2d at 198-199. See generally *Bateman Eichler, Hill Richards*,

Indeed, petitioners assume this to be true for purposes of their discussion of the securities counts in this case (Pet. Br. 10); since they "misappropriated—stole to put it bluntly—valuable nonpublic information entrusted to [them] in the strictest confidence" (*Chiarella*, 445 U.S. at 245 (Burger, C.J., dissenting)), they could hardly contend otherwise. It is equally clear that a fraud of this sort is, vis-a-vis the defrauded party, a "deceptive practice"—a proposition that petitioners also do not contest. Compare *Santa Fe Industries, Inc.* v. *Green*, 430 U.S. 462, 474 (1977) (no deception).

That fraud, moreover—the misappropriation of information for the purpose of trading—plainly occurred "in connection with" petitioners' purchases and sales of securities. Without the fraud their purchases and sales would not have occurred, "at least at the transaction prices." Pet. App. 18a; see *id.* at 19a-20a. Indeed, "the misappropriated information had 'no value whatsoever' * * * except 'in connection with' [petitioners' subsequent purchase[s and sales] of securities" (*id.* at 19a (quoting *Materia*, 745 F.2d at 203)). Thus, "[t]he fraud perpetrated on [Winans'] employer was part and parcel of a larger design, the sole purpose of which was to reap instant no-risk profits in the stock market" (*Materia*, 745 F.2d at 203). See generally *Naftalin*, 441 U.S. at 772-773 & n.4. The court below accordingly found "frivolous" petitioners' contention that the "in connection with" requirement had not been satisfied in this case (Pet. App. 20a), and petitioners have not expressly repeated that contention to this Court.

2. Petitioners nevertheless argue, at length and in a variety of formulations, that their fraud fell outside the "protective zone of section 10(b)" (Pet. Br. 15) because it did not involve breach of "a duty * * * to a market participant" (*id.* at 17).[36] They appear to mean by this

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Inc. v. *Berner*, 472 U.S. 299, 310 (1985); *Huddleston*, 459 U.S. at 388-389.

[36] At various points, petitioners suggest that the victim of a violation of Section 10(b) and Rule 10b-5 must be an "investor[]

assertion either (a) that Section 10(b) and Rule 10b-5 are violated only by classic "insider trading" (in violation of a fiduciary duty owed by a corporate insider to the shareholders of the subject corporation) (see Pet. Br. 17), or (b) that while trading on information misappropriated from a third party may also violate Section 10(b) and Rule 10b-5, it does so only when the third party is itself a market participant (see Pet. Br. 19-20). Both proposed limitations are incorrect.

a. Petitioners' contentions are, first of all, flatly inconsistent with the language of both the statute and the rule. Section 10(b) prohibits the "direct[] or indirect[]" use of "any" deceptive device in connection with the purchase or sale of "any" security. Rule 10b-5 explicitly proscribes "any * * * fraud" committed on "any person." As the Court has explained, these "proscriptions, by statute and rule, are broad and, by repeated use of the word 'any,' are obviously meant to be inclusive." *Affiliated Ute Citizens*, 406 U.S. at 151. See generally *Huddleston*, 459 U.S. at 386-387.

Rather than discuss the language of Section 10(b) or Rule 10b-5,[87] petitioners suggest (see Pet. Br. 13-19) that this Court has effectively limited the reach of Section 10(b) to classic insider trading that violates a fiduciary duty to the person on the other side of the trade. But as the courts below noted (Pet. App. 12a, 57a), the cases

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or person[] engaged in the process of buying or selling stock" (Pet. Br. 14); a person with a role in "the underlying securities transaction" (*ibid.*); a "market participant" (*id.* at 15); or someone "involve[d] in the purchase or sale of securities" (*id.* at 17). But petitioners also evidently realize that the victim of the fraud need not be a purchaser or seller of securities (Pet. Br. 15-16 n.24). That proposition was established by the Court's holding in *United States* v. *Naftalin*, *supra*, that Section 17(a)(1) of the Securities Act—which contains language nearly identical to that of Rule 10b-5—does not "create[] a requirement that injury occur to a purchaser." 441 U.S. at 773.

[87] Not surprisingly, petitioners mention the language of Section 10(b) and Rule 10b-5 only in passing. Their only discussion of the statutory language is the irrelevant suggestion that "manipulation" (which was not alleged in this case) refers to the artificial

upon which petitioners rely for this proposition—*Chiarella* v. *United States*, *supra*, and *Dirks* v. *SEC*, 463 U.S. 646 (1983)—say no such thing. These cases do explain that the liability of a corporate insider or his tippee for trading on nonpublic information is premised on the particular duty of the insider to persons trading in the stock of that corporation, and they hold that there is no liability for trading on disparities in information where there has been *no* breach of *any* duty to *anyone*. See 463 U.S. at 653-654; 445 U.S. at 228-230. See generally *In re Cady, Roberts & Co.*, 40 S.E.C. 907 (1961). But these cases did not purport to "wr[i]te the book on insider and outsider trading; [they] wrote one chapter with respect to one type of fraudulent trading" (Pet. App. 57a).[38] Neither these cases nor any other decision of this Court has suggested that a fraud intentionally practiced on a third party, for the purpose of gaining an unfair advantage in securities trading, violates Section 10(b) only if the per-

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stimulation of market activity for the purpose of misleading investors. Pet. Br. 14 n.22. See generally *Santa Fe Industries*, 430 U.S. at 475-476.

[38] Quoting *Dirks* and *Hochfelder*, petitioners assert that this Court has held that " 'a violation [of Section 10(b)] may be found *only* where there is "intentional or willful conduct designed to deceive or defraud investors by controlling or artificially affecting the price of securities." ' " Pet. Br. 14 (quoting *Dirks*, 463 U.S. at 663 n.23, in turn quoting *Hochfelder*, 425 U.S. at 199) (emphasis added by petitioners). This assertion is highly misleading. The Court in *Hochfelder* made the quoted remark in a discussion of the meaning of the term "manipulation," and nowhere suggested that Section 10(b) does not reach frauds on third parties in connection with securities trading. The Court in *Dirks*, in turn, used the quoted statement while discussing the necessity of scienter in cases involving insider trading. In full, the Court's statement reads: "It is not enough that an insider's conduct results in harm to investors; rather, a violation may be found only where there is 'intentional or willful conduct designed to deceive or defraud investors by controlling or artificially affecting the price of securities.' " 463 U.S. at 663 n.23. Because the fraud in such cases is committed on the insider's trading partners, the Court obviously directed its remarks at fraud on investors.

petrator owes an antecedent duty to his trading partners.[39]

To the contrary, the Court in *Chiarella* expressly noted and left open the possibility that a person who owes no corporate-law duty to the subject corporation's shareholders may violate Section 10(b) and Rule 10b-5 by trading on information misappropriated from a third party. See 445 U.S. at 235-237. Cf. *Bateman Eichler, Hill Richards, Inc.* v. *Berner*, 472 U.S. 299, 313 n.22 (1985). And the four Justices who addressed the validity of this "misappropriation theory" of liability in *Chiarella* concluded that "a person violates § 10(b) whenever he improperly obtains or converts to his own benefit nonpublic information which he then uses in connection with the purchase and sale of securities" (445 U.S. at 239 (Brennan, J., concurring in the judgment)).[40] In the succeeding years,

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[39] Other cases cited by petitioners (Pet. Br. 15-16) either involved the classic insider trading theory or involved limitations, irrelevant here, on private suits brought by injured parties under Rule 10b-5. See page 48, *infra*.

[40] See 445 U.S. at 240 (Burger, C.J., dissenting) ("a person who has misappropriated nonpublic information has an absolute duty to disclose that information or to refrain from trading"); *id.* at 245-246 (Blackmun, J., joined by Marshall, J., dissenting) (expressing general agreement with Chief Justice Burger's views and noting that Chiarella's conversion of confidential information "certainly is the most dramatic evidence that petitioner [is] guilty of fraud"). The majority found it inappropriate to address the validity of the misappropriation theory in *Chiarella* because the theory had not been submitted to the jury. See *id.* at 235-237; *id.* at 238 (Stevens, J., concurring). In Chief Justice Burger's view, an exception to the usual principles of caveat emptor should apply "when an informational advantage is obtained [by one party to a transaction], not by superior experience, foresight, or industry, but by some unlawful means"; in such a case, he would require the party who obtains the information unlawfully to disclose the information or to refrain from trading. *Id.* at 240 (citing Keeton, *supra*, 15 Tex. L. Rev. at 25-26). But cf. *Moss* v. *Morgan Stanley, Inc.*, 719 F.2d 5 (2d Cir. 1983), cert. denied, 465 U.S. 1025 (1984) (dismissing a private action for damages, by investors trading in

this misappropriation theory has received the endorsement both of committees of Congress[41] and of the lower courts, which have consistently upheld application of Section 10(b) and Rule 10b-5 against persons who traded on confidential information fraudulently misappropriated from employers or clients.[42]

The misappropriation theory fills what would otherwise be a large and illogical loophole in the securities laws. A

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the market, against persons who traded on misappropriated information).

Chief Justice Burger's legal theory was that trading on misappropriated information is a wrong not only to the owner of the information but also to the person on the other side of the transaction. Petitioners repeatedly stress that the government did not here allege injury to any trading partner, as if that defeated prosecution. But Chief Justice Burger's theory suggests no such pleading requirement: the relevant point of disagreement in *Chiarella* was whether there was an adequate jury charge of fraudulent *misappropriation* of information. Believing that there was, Chief Justice Burger would have affirmed the conviction under the securities laws on the ground that Chiarella " 'used that information when he knew other people trading in the securities market did not have access to the same information that he had at a time when he knew that that information was material to the value of the stock' " (*Chiarella*, 445 U.S. at 243-244 (quoting jury charge)). Here, the government plainly alleged and proved fraudulent misappropriation of confidential, market-affecting information, and trading on that information without disclosure. It was not necessary for the indictment to explicate the legal theory that such conduct violates the securities laws because of its effect on other investors and the integrity of the market.

[41] The report accompanying the Insider Trading Sanctions Act of 1984, Pub. L. No. 98-376, 98 Stat. 1264, emphasizes that "the abuses sought to be remedied [by Section 10(b)] were not limited to action of corporate insiders" (H.R. Rep. 98-355, 98th Cong., 1st Sess. 5 (1983)), and expressly endorses both the misappropriation theory (see *id.* at 4-5) and decisions applying the theory (see *id.* at 13 n.20). The Court has previously found this report relevant in construing Section 10(b) and Rule 10b-5. See *Bateman Eichler*, 462 U.S. at 313 n.23.

[42] See, *e.g.*, *SEC* v. *Materia*, *supra*; *United States* v. *Newman*, *supra*; *SEC* v. *Gaspar*, [1984-1985] Fed. Sec. L. Rep. (CCH) ¶ 92,004 (S.D.N.Y. Apr. 15, 1985); *SEC* v. *Musella*, 578 F. Supp. 425 (S.D.N.Y. 1984).

person who trades on information that he fraudulently misappropriated from a takeover bidder, from an investment banker analyzing a possible acquisition for a client, or for that matter from any entity other than the corporation whose stock is being traded, is ordinarily not a corporate insider of that corporation (or an insider's tippee) and ordinarily has no insider's duty of disclosure to the stockholders of that corporation. See generally *Dirks*, 463 U.S. at 659. In such cases—which unfortunately occur with some frequency [43]—the theory of the prosecution is that trading on fraudulently misappropriated information violates Section 10(b) even if the defendant is not an insider and the information does not originate in the target company.[44]

The misappropriation theory does more than follow from a literal reading of Section 10(b) and Rule 10b-5. It also furthers the central purpose of the Exchange Act:

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[43] For recent cases based at least in part on the misappropriation theory, see, *e.g.*, *SEC* v. *Siegel*, No. 87 Civ. 0963 (S.D.N.Y. Feb. 13, 1987) (disgorgement of $4.3 million in illegal profits and other assets); *SEC* v. *Boesky*, No. 86 Civ. 8767 (S.D.N.Y. Nov. 14, 1986) (disgorgement of $50 million in illegal profits and $50 million penalty); *SEC* v. *Tome*, 638 F. Supp. 596 (S.D.N.Y. 1986), appeal pending No. 86-6192(L) (2d Cir.) (disgorgement of $2.7 million in illegal profits); *SEC* v. *Levine*, No. 86 Civ. 3726 (S.D.N.Y. June 5, 1986) (disgorgement of $11.6 million in illegal profits).

[44] In certain situations, Rule 14e-3, 17 C.F.R. 240.14e-3, promulgated under Section 14(e) of the Exchange Act, 15 U.S.C. 78n(e), prohibits trading while in possession of material nonpublic information relating to a tender offer that has been acquired from the offeror, the target, or any agent or employee of either party. In such situations, trading may violate both Rule 10b-5 and Rule 14e-3. But Rule 14e-3 does not reach cases where the information does not concern a tender offer (but instead, for example, a merger), or where the source of the information is not a party to a tender offer. Noting the limits of Rule 14e-3, one commentator has suggested the example of "a judicial clerk [who sells] shares of a particular company on the basis of his knowledge that a huge judgment would soon be rendered against it." Aldave, *Misappropriation: A General Theory of Liability for Trading on Nonpublic Information*, 13 Hofstra L. Rev. 101, 106 n.33 (1984).

"to insure the maintenance of fair and honest markets in [securities] transactions." 15 U.S.C. 78b.[45] In its first consideration of a private civil action under Rule 10b-5, the Court noted that basic purpose of Section 10(b) is "'preserving the integrity of the securities market'" (*Bankers Life*, 404 U.S. at 12 (citation omitted)), a goal that serves the interests both of individual investors and of the market as a whole. See *Naftalin*, 441 U.S. at 776. The only specific legislative history of Section 10(b), the Exchange Act's catchall antifraud provision, confirms that the clause had the equally broad purpose of eliminating from the securities markets all "manipulative and deceptive practices which have been demonstrated to fulfill no useful function." S. Rep. 792, 73d Cong., 2d Sess. 6 (1934). Section 10(b) (emphasis added) thus expressly authorizes the Commission to adopt rules that are "necessary or appropriate in the public interest *or* for the protection of investors."

The present case dramatically illustrates the damage to the "public interest" that flows from the use of fraudulently misappropriated information in securities trading. As the court of appeals observed with some understatement, there was nothing "'useful' about [petitioners'] scheme" (Pet. App. 13a); their "information advantage [was] obtained by conversion and not by legitimate economic activity that society seeks to encourage" (*Chiarella*, 445 U.S. at 242 n.3 (Burger, C.J., dissenting)). See *id.* at 241. Compare *Dirks*, 463 U.S. at 658-659. Such conduct has a profoundly negative effect on the functioning of the securities markets. It is a commonplace—often noted by commentators, by those involved in regulation of the markets, and by committees of Congress—that

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[45] As the House Committee explained in connection with the major amendments to the Exchange Act in 1975: "The basic goals of the Exchange Act remain saluta[]ry and unchallenged: To provide fair and honest mechanisms for the pricing of securities, to assure that dealing in securities is fair and without undue preference or advantages among investors * * * and to provide, to the maximum degree practicable, markets that are open and orderly." H.R. Conf. Rep. 94-229, 94th Cong., 1st Sess. 91-92 (1975).

"[t]he abuse of informational advantages that other investors cannot hope to overcome through their own efforts is unfair and inconsistent with the investing public's legitimate expectation of honest and fair securities markets where all participants play by the same rules." H.R. Rep. 98-355, *supra*, at 5.[46] The use of illegally acquired information to obtain an advantage in trading thus "undermin[es]" public confidence in the honesty of securities transactions, inevitably driving investors out of the market and threatening both "[c]apital formation and our nation's economic growth and stability." *Id.* at 2. See 129 Cong. Rec. S3865 (daily ed. Mar. 23, 1983) (remarks of Sen. D'Amato; 130 Cong. Rec. H7759 (daily ed. July 25, 1984). (remarks of Rep. Wirth); ABA Committee on Federal Regulation of Securities, *Report of the Task Force on Regulation of Insider Trading—Part I: Regulation Under the Antifraud Provisions of the Securities Exchange Act of 1934*, 41 Bus. Law. 223, 227-228 & n.8 (1985).[47]

Trading on fraudulently misappropriated information also, of course, injures investors, both individually and as a class. Petitioners, for example, exploited the information they misappropriated "for [their own] financial benefit * * * and to the financial detriment of those investors with whom [they] traded"; "those who pur-

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[46] See ABA Committee on Federal Regulation of Securities, *supra*, 41 Bus. Law. at 227; Brudney, *Insiders, Outsiders, and Informational Advantages Under the Federal Securities Laws*, 93 Harv. L. Rev. 322, 346 (1979); Aldave, *supra*, 13 Hofstra L. Rev. at 122-123.

[47] As the Insider Trading Task Force of the ABA Committee on Federal Regulation of Securities observed, "people will not entrust their resources to a marketplace they don't believe is fair, any more than a card player will put his chips on the table in a poker game that may be fixed. Although the task force knows of no empirical research that directly demonstrates that concerns about integrity affect market activity, both authoritative commentators and common sense tell us that if investors do not anticipate fair treatment, they will avoid investing in securities. As a result, capital formation through securities offerings will become less attractive and more difficult." 41 Bus. Law. at 227-228 (footnote omitted).

chased or sold securities without the misappropriated information would not have purchased or sold, at least at the transaction prices, had they had the benefit of that information" (Pet. App. 18a). More broadly, as the Court has observed, the well-being of investors is inextricably linked to the health of the market and of the economy as a whole. See *Naftalin*, 441 U.S. at 776. Petitioners' conduct inflicted a wound on the market and all of the participants in it.

b. Petitioners themselves appear at various points (see, *e.g.*, Pet. Br. 19) to concede that trading on fraudulently misappropriated information may violate Rule 10b-5. They seem to recognize, for example, that trading on information misappropriated from a takeover bidder is unlawful, even when the defendant traded neither with the bidder nor in the bidder's shares (*id.* at 19-20). They argue, however, that while trading on confidential information misappropriated from a "market participant" may violate Section 10(b) and Rule 10b-5, the identical use of similar information purloined from a market *observer* such as the Journal does not (see Pet. Br. 19-22).

Petitioners offer absolutely no justification for their stopping place for Section 10(b) liability—which finds no support in the language of the statute or Rule 10b-5—beyond the bald assertion that the first category of these frauds falls within, and the second without, the "protective zone of [Section] 10(b)" (Pet. Br. 15).[48] But a principal purpose of the Exchange Act as a whole, and

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[48] Relying on the dissenting opinion below, petitioners do argue that the misappropriated information here did not involve " 'special securities-related knowledge' " (Pet. Br. 21 (quoting Pet. App. 29a)). As the court of appeals noted, however, the information taken by petitioners unquestionably was material; the *Heard* column had immediate effects on the market prices of the securities that it discussed (Pet. App. 19a n.9). See *TSC Industries, Inc.* v. *Northway, Inc.*, 426 U.S. 438, 449 (1976). Petitioners themselves obviously believed that their advance knowledge of the Journal's publication plans was significant, for their entire scheme was premised on their ability to trade securities prior to publication and then to profit from the market's response.

of the misappropriation doctrine in particular, is to foster orderly competition for information, guarantee honest markets, and maintain investor confidence. See pages 43-46, *supra*. The fact that the *owner* of the purloined information is not itself trading has absolutely no bearing on the fact that the thief who does trade on that information is corrupting the trading process, creating a disincentive to research and analysis, gaining an improper advantage over honest investors, and discouraging those investors from participating in the market. It is hardly a novel idea that the deception of one person may also, in this way, injure others.[49] Here, petitioners' fraud not only harmed the Journal but also damaged the integrity of the market as a whole. Conduct that can cause such damage must, to use petitioners' language, fall within the "zone" proscribed by Section 10(b).

Certainly, trading on information misappropriated from a takeover bidder or other securities trader also violates Section 10(b) and Rule 10b-5 in connection with *that person's* purchases and sales of securities. See, *e.g.*, *Newman*, 664 F.2d at 17-18. But both a "connection" with purchases or sales of securities and a fundamental harm to the integrity of the market are present *whenever* trading is based on fraudulently misappropriated information. Petitioners' proposed limitation of misappropriation liability to cases where the owner of the information is injured in respect of *its* trading would, to take just one example, lead to the absurd conclusion that trading on information misappropriated from an investment banker is outside the "zone" of conduct regulated by Section 10(b) whenever the information belongs to the investment banker and not to a market participant.

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[49] See, *e.g.*, *Bohannon* v. *Wachovia Bank & Trust Co.*, 210 N.C. 679, 188 S.E. 390 (1936) (testator deceived into disinheriting plaintiff); *Mitchell* v. *Langley*, 143 Ga. 827, 85 S.E. 1050 (1915) (holder of life insurance policy fraudulently induced to change beneficiaries). See generally Aldave, *supra*, 13 Hofstra L. Rev. at 120.

Of course, only a purchaser or seller of securities may bring a suit for damages under Rule 10b-5's judicially created private right of action, and such a plaintiff must prove injury to himself. See *Blue Chip Stamps* v. *Manor Drug Stores*, 421 U.S. 723 (1975). But limitations on the recovery of damages in private suits are grounded on considerations of policy that have no application in actions brought by enforcement authorities to vindicate the public interest. See *id.* at 740-747; *id.* at 757-760 (Powell, J., concurring). Indeed, the Court has expressly indicated that the purchaser-seller limitation "is inapplicable" in criminal prosecutions or SEC civil enforcement actions for securities fraud. *Naftalin*, 441 U.S. at 774 n.6. See *Blue Chip Stamps*, 421 U.S. at 753 n.14; *SEC* v. *National Securities, Inc.*, 375 U.S. 453, 467 n.9 (1969). In such cases, " 'the precise direction in which a duty may have been owed' " (*Materia*, 745 F.2d at 202 (citation omitted)) is immaterial so long as deceitful conduct was practiced, "directly or indirectly," in connection with the purchase and sale of securities.[50]

3. Petitioners' remaining contentions also lack merit. There would be nothing anomalous in the application of Rule 10b-5 to petitioners even if it were true, as they assert (Pet. Br. 22), that Dow Jones could have traded

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[50] Petitioners place considerable reliance (Pet. Br. 15) on then-Judge Stevens' opinion for the Seventh Circuit in *Eason* v. *General Motors Acceptance Corp.*, 490 F.2d 654, 659 (1973), cert. denied, 416 U.S. 960 (1974), for the proposition that a violation of Rule 10b-5 occurs only when the injured party is an "investor." Because the injured party in that case was in fact an investor, however, and because the action was a private suit for damages, there was no reason for the court of appeals in *Eason* to determine whether, in a government enforcement action, the victim of the fraud must have been an investor. Indeed, Justice Stevens has explained more recently that "the limitation on the right to recover pecuniary damages in a private action [under Rule 10b-5] * * * is not necessarily coextensive with the limits of the rule itself." *Chiarella*, 445 U.S. at 238 (Stevens, J., concurring). And the Court's decision in *United States* v. *Naftalin*, *supra*, makes clear that a securities fraud need not be directed at a purchaser or seller—or, for that matter, at an investor. See note 36, *supra*.

on *its* knowledge of forthcoming *Heard* columns.[51] As the court of appeals noted (Pet. App. 21a), petitioners' argument "illogically casts the thief and [his] victim in the same shoes." There are, of course, situations in which it is perfectly proper for the owner to trade on information that a thief may not use in trading; for example—as petitioners appear to acknowledge (Pet. Br. 19-20)—a tender offeror may make pre-announcement purchases of target company stock for its own account (although the Williams Act, 15 U.S.C. 78m(d)(1), imposes post-purchase disclosure requirements), but an employee of the offeror (or its printer) commits a fraud if he misappropriates information about the offeror's plans in order to trade for himself. See *Chiarella*, 445 U.S. at 240 (Burger, C.J., dissenting); *Materia*, 745 F.2d at 201-203.[52] Here,

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[51] In fact, the court of appeals expressly left open the question whether that pre-publication trading by a financial newspaper would work a fraud under a different legal theory than the one involved in this case (Pet. App. 20a n.10). Cf. *Zweig* v. *Hearst Corp.*, 594 F.2d 1261 (9th Cir. 1979) (scalping theory of liability under Rule 10b-5); *SEC* v. *Blavin*, 557 F. Supp. 1304 (E.D. Mich. 1983), aff'd, 760 F.2d 706 (6th Cir. 1985) (scalping) (both cited with apparent approval in *Lowe* v. *SEC*, 472 U.S. 181, 209-210 n.56 (1985)).

[52] As the court of appeals explained, the misappropriation theory does not at all suggest a "parity of information" rule (Pet. App. 15a-16a). To the contrary, prohibiting trading on misappropriated information encourages lawful competition for superior knowledge and insight, which is essential to the market's functioning. See *Dirks*, 463 U.S. at 658-659. While someone may trade on superior information gained in any number of legal ways, it is improper to obtain such an informational advantage by "misappropriating material nonpublic information in breach of an employer-imposed fiduciary duty of confidentiality" (Pet. App. 16a).

If the Journal had expressly permitted its employees to trade on confidential information, Winans' actions obviously would not have amounted to a fraud on his employer (although a publication that allowed its employees to engage in such conduct would soon lose the reputation for reliability and integrity that makes the information valuable in a scheme such as the one here). We note, however, that the simple absence of an express policy like the Journal's would not justify employee trading, since, as the court

on the other hand, it would have been unethical and against its self-interest (as reflected in the rules that Winans broke), for Dow Jones to have traded on information about its publication schedule, but there is no anomaly in relying on the owner's integrity and self-interest to deter its misuse of its own information, while prohibiting such misuse by a thief.

Petitioners' further contention that they lacked notice of the illegality of their conduct (Pet. Br. 23-28) is simply incorrect. In fact, the district court specifically found that Felis "understood" that he was involved in "an unlawful venture" (Pet. App. 71a), and the court found generally that petitioners were aware that their acts were wrongful (*id.* at 69a). They surely " 'would have [been] most ingenuous' " to have believed otherwise (*ibid.* (citation omitted)). Notwithstanding petitioners' rhetorical questions (see Pet. Br. 25-26), it has long been the law that deceitful use of confidential information obtained from an employer is unlawful in a variety of settings. See *Newman*, 664 F.2d at 18 (citing cases). By the time of petitioners' scheme, the Second Circuit had expressly so ruled in *Newman* itself, a case involving Section 10(b) and Rule 10b-5. See also Pet. App. 22a (citing cases).[53] Petitioners are hardly entitled to immunity because their scheme differed in some particulars from the ones previously prosecuted: "that there is no litigated fact pattern precisely in point may constitute a tribute to the cupidity and ingenuity of the malefactors involved but hardly provides an escape from the penal sanctions of the securities fraud provisions."

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below recognized (Pet. App. 10a n.5), the common law itself imposes duties on employees not to use their employer's confidential information to the employer's detriment. See note 13, *supra*.

[53] Indeed, a congressional report on trading abuses issued shortly before petitioners began to trade on the Journal's information cited the Second Circuit's decision in *United States* v. *Newman*, *supra*, as having helped "clarif[y] the legal principles governing * * * cases that involve trading on information that originates from sources other than the company [whose shares are being traded]." H.R. Rep. 98-355, *supra*, at 13 n.20.

United States v. *Brown*, 555 F.2d 336, 339-340 (2d Cir. 1977).[54]

CONCLUSION

The judgment of the court of appeals should be affirmed.

Respectfully submitted.

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[54] Finally, we note that the suggestion of *amici* Reporters Committee for Freedom of the Press, *et al.*, that the prosecution here somehow raises First Amendment concerns (Br. 19-25) is preposterous. A generally applicable criminal law can constitutionally be applied to a criminal whose nominal profession is journalism. A newspaper might be "chilled" (see Br. 22) in deciding whether to publish a given article because publication would reveal that its reporter committed burglary to obtain the information on which the article is based, but that hardly makes burglary laws unconstitutional as applied to members of the press. Section 10(b) and Rule 10b-5 similarly create a general prohibition against the fraudulent use of an employer's confidential information in connection with the purchase or sale of securities, and there is no reason to exempt reporters from this requirement. Affirmance of the decision below will discourage reporters from doing only one thing: committing securities fraud. We also note that amici's wildly unrealistic hypothetical (Br. 20-21) has nothing to do with the issues in this case; the only editorial decision affected by Winans' fraud was Winans' quick departure from the Journal.

STATUTORY APPENDIX

Section 10(b) of the Securities Exchange Act of 1934, 15 U.S.C. 78j(b), provides:

> It shall be unlawful for any person, directly or indirectly, by the use of any means or instrumentality of interstate commerce or of the mails, or of any facility of any national securities exchange—
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> * * * *
>
> (b) To use or employ, in connection with the purchase or sale of any security registered on a national securities exchange or any security not so registered, any manipulative or deceptive device or contrivance in contravention of such rules and regulations as the [Securities and Exchange] Commission may prescribe as necessary or appropriate in the public interest or for the protection of investors.

18 U.S.C. 371 provides:

> If two or more persons conspire either to commit any offense against the United States, or to defraud the United States, or any agency thereof in any manner or for any purpose, and one or more of such persons do any act to effect the object of the conspiracy, each shall be fined not more than $10,000 or imprisoned not more than five years, or both.

18 U.S.C. 1341 provides:

> Whoever, having devised or intending to devise any scheme or artifice to defraud, or for obtaining money or property by means of false or fraudulent pretenses, representations, or promises, or to sell, dispose of, loan, exchange, alter, give away, distribute, supply, or furnish or procure for unlawful use any counterfeit or spurious coin, obligation, secu-

rity, or other article, or anything represented to be or intimated or held out to be such counterfeit or spurious article, for the purpose of executing such scheme or artifice or attempting to do so, places in any post office or authorized depository for mail matter, any matter or thing whatever to be sent or delivered by the Postal Service, or takes or receives therefrom, any such matter or thing, or knowingly causes to be delivered by mail according to the direction thereon, or at the place at which it is directed to be delivered by the person to whom it is addressed, any such matter or thing, shall be fined not more than $1,000 or imprisoned not more than five years, or both.

18 U.S.C. 1343 provides:

Whoever, having devised or intending to devise any scheme or artifice to defraud, or for obtaining money or property by means of false or fraudulent pretenses, representations, or promises, transmits or causes to be transmitted by means of wire, radio, or television communication in interstate or foreign commerce, any writings, signs, signals, pictures, or sounds for the purpose of executing such scheme or artifice, shall be fined not more than $1,000 or imprisoned not more than five years, or both.

17 C.F.R. 240.10b-5 provides:

It shall be unlawful for any person, directly or indirectly, by the use of any means or instrumentality of interstate commerce, or of the mails or of any national securities exchange,

(a) To employ any device, scheme, or artifice to defraud,

(b) To make any untrue statement of a material fact or to omit to state a material fact necessary in order to make the statements

made, in the light of the circumstances under which they were made, not misleading, or

(c) To engage in any act, practice, or course of business which operates or would operate as a fraud or deceit upon any person,

in connection with the purchase or sale of any security.

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